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Politics this week

Jun 25th 2009
From The Economist print edition

Getty Images

Iran's street protests in the wake of a disputed presidential election spread from Tehran, the capital, to a string of big cities across the country, but then seemed to subside after the authorities cracked down, leaving at least 20 people dead. A young woman, Neda Agha Soltan, became a symbol of the protests after her dying moments were posted on the internet. Discord within the upper ranks of the clerical establishment ensured that the crisis was by no means over. See article

With American troops due to withdraw from all **Iraqi** towns at the end of the month, insurgents carried out a campaign of bombings. On June 20th at least 70 people were killed by a truck bomb in Taza, a Turkmen town just south of the disputed city of Kirkuk. Two days later at least seven bombs went off in and around Baghdad, killing over 30 people. Two days after that another bomb attack, in a Shia part of the city, killed more than 70 people. See article

Somalia's fragile government called in vain on its neighbours, Ethiopia and Kenya, to send troops to help it resist a growing jihadist insurgency bolstered by al-Qaeda-linked fighters from Pakistan and Afghanistan. But it was reported that the United States had secretly begun to resupply the Somali government. See article

Farm hands

Democrats working on America's **climate-change** legislation in the House struck a deal that gives the Department of Agriculture the authority to supervise efforts to reduce carbon emissions by farmers. With little Republican backing, Democratic leaders had to secure the support of colleagues from rural districts.

Mark Sanford, the Republican governor of **South Carolina**, caused a stir when he disappeared for five days. His staff said he had gone hiking in the Appalachians. In fact, Mr Sanford had been in Argentina. On his return he admitted to an extramarital affair with a woman there.

Antonio Villaraigosa ruled himself out of the running for governor of **California**. The mayor of Los Angeles had been tipped to enter the field of candidates seeking to succeed Arnold Schwarzenegger.

AP

Two Metro trains collided in **Washington, DC**, killing nine people, the worst-ever accident on the city's network.

Battle ready

At least 80 people were killed in an attack by an unmanned American aircraft in **the tribal areas of Pakistan**. The attack was in South Waziristan, the stronghold of Baitullah Mehsud, leader of the Pakistani Taliban, and came as the Pakistani army prepared a new offensive in the area.

America reached an agreement with **Kyrgyzstan** that will allow American armed forces to continue using the Manas air base, their only base in Central Asia, to support operations in Afghanistan. In February the government had insisted the base must close.

An American journalist from the *New York Times* and an Afghan colleague were reported to have escaped after seven months as prisoners of the Taliban, who took them hostage in **Afghanistan**. Their driver is still being held. They regained their freedom in North Waziristan, in Pakistan.

Formal charges were announced against Liu Xiaobo, one of **China's** most prominent dissidents, who was detained last December after the publication of a charter calling for political reform.

An American navy ship continued to track a **North Korean** vessel believed to be carrying weapons to Myanmar in breach of UN sanctions. North Korea boasted of being a "proud nuclear power" and was believed to be poised to anger the outside world further with a new missile test. See article

A conservation group reported that 30% of the world's species of **sharks** are under threat of extinction because of overfishing. Shark meat and liver oil are becoming more popular, and demand remains high in Asia for shark fins.

Drugs run

The UN's annual report on illicit **drugs** found significant reductions in the production of cocaine, opium and cannabis, but an increase in the output of synthetic substances, such as ecstasy and methamphetamine. Cocaine cultivation fell by 18% in Colombia, the world's biggest producer of the drug. See article

A battle between FARC rebels and security forces in **Colombia's** Cauca province killed at least 25 rebels and seven police officers. Authorities said that a local FARC commander known as *El Enano* (the Midget) was among the dead.

The **United States** and **Venezuela** decided to reinstate their ambassadors. Venezuela's envoy was expelled by America last September after it alleged that America was plotting to overthrow Evo Morales, the Bolivian president. Venezuela then threw out America's man.

Clothing maketh the man

In a rare address to both houses of **France's** parliament, President Nicolas Sarkozy lent weight to a possible ban on the Islamic burqa, saying that such garments were "not welcome on French territory". See article

Yunus-Bek Yevkurov, the president of Ingushetia, a Russian republic in the **north Caucasus**, was almost killed in an assassination attack by a suicide-bomber. Ingushetia, next to Chechnya, has recently become the most violent place in the north Caucasus.

Russia's Supreme Court ordered a retrial of three men acquitted of being accomplices in the murder of Anna Politkovskaya, a crusading journalist whom Vladimir Putin described as a "marginal" figure. None of the men are accused of the actual killing.

A former prime minister of **Kosovo**, Agim Ceku, was arrested in Bulgaria. He is wanted by Serbia on war-crimes charges.

Sex scandals continued to swirl around **Italy's** prime minister, Silvio Berlusconi. Magistrates are investigating a possible call-girl ring, some members of which allegedly visited Mr Berlusconi in Rome. See article

Adam Roberts

Two tonnes of rare whale meat were distributed in **Greenland** as part of celebrations to mark the start of an era of self-government. After nearly three centuries of rule by Denmark, Greenland's 56,000 people will gradually take control of most domestic affairs, although defence and foreign policy remain in Danish hands. Greenlandic is now the official language.

Business this week

Jun 25th 2009
From The Economist print edition

Xstrata's all-share offer to **Anglo American** for a "merger of equals" was forcefully rebuffed by Anglo's board. Big investors in Anglo urged it to keep the door open to a sweetened deal, which would create the world's third-biggest mining company. See article

Addax Petroleum agreed to an C$8.3 billion ($7.2 billion) takeover from **Sinopec**, giving the Chinese state-controlled oil firm access to Addax's operations exploring off the West African coast and developing the Taq Taq field in Iraq. The deal comes shortly before the Iraqi government prepares to auction off oil contracts to foreign companies. See article

America and the European Union lodged a complaint with the World Trade Organisation alleging that China is placing unfair levies on its exports of **raw materials**, such as bauxite and zinc, thereby providing cheaper materials to manufacturers at home. See article

Any dream will do

Boeing yet again postponed the maiden test flight of its **787 Dreamliner**, this time because of structural weakness in the area where the wing attaches to the body of the aeroplane. The company had only recently insisted that the flight would take place by the end of the month. A new timetable will be announced within the next few weeks for the project, which is already two years behind schedule. See article

The **European Central Bank** provided a record €442 billion ($620 billion) to the euro area's banking system through its offer of unlimited one-year funds at 1% interest. The measure has been dubbed a "stimulus by stealth".

The **World Bank** predicted that the economies of the developing countries would grow by only 1.2% this year, significantly below last year's growth rate of 5.9%. By contrast, the **OECD** raised its forecast of economic growth for the first time in two years. The Paris-based organisation of 30 industrialised countries now expects GDP among its members to contract by 4.1% in 2009 and to grow by a modest 0.7% in 2010.

The **Federal Reserve** sounded a bit more optimistic about the American economy than it has for a while. After a two-day meeting, the Fed said that the "pace of economic contraction is slowing", though the economy would "remain weak for a time". The central bank played down the threat from deflation, a threat it had emphasised earlier this year.

Beware of the bear

Russian **stockmarkets** fell further when the World Bank forecast Russia's economy would shrink by 7.9% this year. Russian indices have tumbled this month from their previous highs for the year, as have stockmarkets in many emerging economies. (China's stockmarkets bucked the trend by reaching their highest levels for a year.) Analysts have sounded a note of caution about American and European stockmarkets, too, warning that underlying economic fundamentals are not as strong as the rallies of the past three months would suggest.

Apple said it sold 1m of its next-generation iPhone 3GS handsets during the first weekend the device was on sale. The figure was higher than most had expected, providing a fillip to **Steve Jobs** as he prepared to return to the helm after six months of medical leave. This did not stop investors from speculating about the health of Apple's chief executive, who recently underwent a liver transplant.

MySpace announced more job cuts. After drastically reducing the size of its American workforce, the social-networking website slashed its international staff by two-thirds as it adapts to a sharp decline in advertising revenue.

Kohlberg Kravis Roberts adjusted its plan to turn itself into a public company by proposing an offering through a merger with an affiliate already listed on the Euronext exchange. The “back door” move is viewed as a stepping stone to an eventual listing on the New York Stock Exchange.

Let shareholders supervise?

Royal Bank of Scotland was embroiled in more controversy over executive pay when it emerged that Stephen Hester, its chief executive, would receive a compensation package worth up to £9.6m ($15.8m). The package was backed by the bank’s institutional shareholders to “incentivise” Mr Hester. His predecessor, Sir Fred Goodwin, only recently agreed to return half of his £700,000 annual pension after a public outcry.

The number of people with net assets of at least $1m (excluding their homes) fell by 14.9% in 2008, according to an annual report from Capgemini and Merrill Lynch. The total wealth of these 8.6m **“high net-worth individuals”** stood at $32.8 trillion. Over half of the super-rich live in America, Japan and Germany, but China passed Britain to take fourth place for the first time.

KAL's cartoon

Jun 25th 2009
From The Economist print edition

Illustration by KAL

This is going to hurt

Jun 25th 2009
From The Economist print edition

Barack Obama was elected in part to fix America’s health-care system. Now is the time for him to keep his word

Getty Images

DIAGNOSING what is wrong with America’s health-care system is the easy part. Even though one dollar in every six generated by the world’s richest economy is spent on health—almost twice the average for rich countries—infant mortality, life expectancy and survival-rates for heart attacks are all worse than the OECD average. Meanwhile, because health insurance is so expensive, nearly 50m Americans, an obscene number in such a rich place, have none; those that are insured pay through the nose for their cover, and often find it bankruptingly inadequate if they get seriously ill or injured.

The costs of health care hurt America in three other ways. First, since half the population (most children, the very poor, the old, public-sector workers) get their health care via the government, the burden on the taxpayer is heavier than it needs to be, and is slowly but surely eating up federal and state budgets. Second, private insurance schemes are a huge problem for employers: the cost of health insurance helped bring down GM, and many smaller firms are giving up covering employees. Third, expensive premiums depress workers’ wages.

Every rich country faces some of these problems (see article), but nobody suffers worse from them than America. This summer’s debate about health care may determine the success of Barack Obama’s presidency. What should he do?

Uncomfortably numb

If he were starting from scratch, there would be a strong case (even to a newspaper as economically liberal as this one) for a system based mostly around publicly funded health care. But America is not starting from scratch, and none of the plans in Congress shows an appetite for such a European solution. America wants to keep a mostly private system—but one that brings in the uninsured and cuts costs. That will be painful, and require more audacity than Mr Obama has shown so far.

The uninsured are the relatively straightforward bit. All you need do is “mandate” everyone to take out health insurance, much as drivers are legally required to have car insurance. Poorer Americans would get subsidies, and (as with car insurance) insurance-providers would be forced to offer affordable plans and not exclude the sick or the old. This has already happened in Massachusetts as well as in a raft of countries, including the Netherlands, Israel and Singapore. All the main proposals now working their way through

Congress include some version of a mandate. Mr Obama opposed a mandate on the campaign trail, but since he has not come up with any plausible alternative, he should quietly swallow one.

The snag is that all these subsidies are expensive. Those congressional plans might cost $1.2 trillion to $1.6 trillion over ten years: the White House is feverishly trying to massage the estimates downward, as well as working out how to plug the hole through various savings and tax increases. But the sticker-shock for the mandate is really just a reflection of the second big problem: the overall cost structure of American health care. Indeed, one of the worst things about Mr Obama's oddly hands-off approach to health reform (see article) is that he is concentrating on a symptom, not the underlying disease.

A bolder president would start by attacking two huge distortions that make American health care more expensive than it needs to be. The first is that employer-provided health-care packages are tax-deductible. This is unfair to those without such insurance, who still have to subsidise it via their taxes. It also encourages gold-plated insurance schemes, since their full cost is not transparent. This tax break costs the government at least $250 billion a year. Mr Obama still shies away from axing it, as do the main congressional plans on offer; but it ought to go (albeit perhaps in stages).

Perversity on stilts, or crutches

The second big distortion is that most doctors in America work on a fee-for-service basis; the more pills they prescribe, or tests they order, or procedures they perform, the more money they get—even though there is abundant clinical evidence that more spending does not reliably lead to better outcomes. Private providers everywhere are vulnerable to this perverse incentive, but in America, where most health care is delivered by the private sector rather than by salaried public-sector staff, the problem is worse than anywhere else.

The trouble is that many Americans are understandably happy with all-you-can-eat health care, which allows them to see any doctor they like and get any test that they are talked into thinking they need. Forcing people into “managed” health schemes, where some species of bureaucrat decides which treatments are cost-effective, is politically toxic; it was the central tenet of Hillary Clinton's disastrous failed reform in 1994.

But to some extent it will have to be done. There is solid evidence to suggest that by cutting back on unnecessarily expensive procedures and prescriptions, anything from 10% to 30% of health costs could be saved: a gigantic sum. The Mayo Clinic in Minnesota and the California-based Kaiser Permanente system have shown that it is possible to save money and produce better outcomes at the same time. So reform must aim to encourage more use of managed health care, provided by doctors who are salaried, or paid by results rather than for every catheter they insert. Medicare, the government-run insurance scheme for those over 65, could show the way, by making much more use of results-based schemes and encouraging more competition among its various providers and insurers.

But in the end it will be up to the private health-care system. One thing that should be unleashed immediately is antitrust: on a local level many hospitals and doctors work as price-fixing cabals. Another option, favoured by many Democrats and the president, is for the government to step in with a results-based plan of its own, to compete against the private industry. That could harm innovation and distort the market further. Mr Obama should use it as a threat, rather than implement it now. If the private sector does not meet certain cost-cutting targets in, say, five years, a public-sector plan should automatically kick in. Such a prospect would encourage hospitals and doctors to accept a painful but necessary reform now.

Germany's inscrutable chancellor

The mystery of Mrs Merkel

Jun 25th 2009
From The Economist print edition

Europe’s canniest politician needs to be bolder about reform if she is to be seen as an historic chancellor

Reuters

SHE is the first female leader of Germany and the first since the war to hail from the east. She has had the job for three-and-a-half years and looks likely to keep it after the federal election in September. Yet as Angela Merkel prepared to meet Barack Obama in Washington this week, a certain mystery still hung over her. Who is she and where might she take her country?

Mrs Merkel’s character is best summed up by what she is not. Unlike other European leaders, she is neither charismatic, nor flashily intellectual, nor domineering. Yet nobody could deny that she is a highly effective politician. She has swatted aside all challengers inside her Christian Democratic Union (CDU), despite coming from outside the party’s traditional base. She has grabbed any credit going for her “grand coalition” with the Social Democratic Party (SPD), leaving her SPD rival for the chancellorship floundering. She won kudos for her presidencies of the European Union and the G8 club of rich countries in 2007. Were she to express interest in the job of EU president that will be created if the EU’s Lisbon treaty is ratified this autumn, it would be given to her on a plate.

Above all, Mrs Merkel has stayed popular—more consistently so than any chancellor since Konrad Adenauer. And she has accomplished this in the teeth of Germany’s worst recession since the war. GDP shrank by 7% in the year to the first quarter. Industrial production has fallen by over a fifth. Unemployment has been masked by job subsidies and make-work schemes, but it is likely to climb back above 4m next year. That Mrs Merkel is still favourite to win re-election as chancellor, whether in another grand coalition or with the liberal Free Democratic Party (FDP), is a tribute to her political skill.

But is she a reformer?

The question is not whether Mrs Merkel will keep power, but whether she is ready to use it. She has an unusual background for a CDU leader: daughter of a Protestant pastor, raised in communist East Germany, she was a physicist before turning to politics (see article). That ought to bode well in a party that is fonder of consensus than of radical change. She seems intellectually to accept the case for greater liberalisation, smaller government and freer markets. But she has shrunk from more substantial reform, for four reasons.

First, she is cautious by temperament. The opposite of France’s Nicolas Sarkozy, she is more of a methodical scientist than a mercurial revolutionary. Those who once hoped that she might be a Thatcherite reformer, a Maggie from Mecklenburg, were always going to be disappointed. Moreover, her instinctive

caution was reinforced by a second factor: her experience in the 2005 election campaign. When her then economic adviser started talking of big tax cuts and radical welfare reforms, her support dropped sharply—and even after she dumped him and tacked back to the centre, she almost lost.

That led to the third and most obvious reason why Mrs Merkel has been unable to be radical: her narrow victory forced her into a grand coalition. Such an alliance operates by the lowest common denominator. Mrs Merkel has held it together, but at the cost of putting off serious talk of most further reforms to the labour market, the welfare state, health-care financing and a hugely complex tax system. The only substantive measure her government has adopted is a rise in the retirement age. Her SPD partners have even managed to roll back some of the Agenda 2010 reforms they made when they were previously in coalition with the Greens in 2003-04.

That also reflects a fourth explanation for Mrs Merkel's lack of reformist zeal, which is the mood of her country. Germany is a place built on consensus—in the workplace, in society and in politics. It is also successful. It is still (just) the world's biggest exporter; thanks to impressive discipline over wages, its companies have regained competitiveness; and its public finances are in better shape than most. The angst of a decade ago, when it seemed that Germany might be the new sick man of Europe, has largely gone. Instead, the global economic crash is seen in Germany as something that came entirely from outside because of Anglo-Saxon free-market zealots—and that has not made Germans any keener on further liberalisation.

Yet all this betrays a dangerous complacency. Even if the economic crisis was not made in Germany, it has changed the world: Germany will suffer unless it responds. The old reliance on manufacturing exports looks broken. Consumers, chary of spending, are hobbling domestic demand. Services, the backbone of all modern economies, are underdeveloped. Germany suffers from deeper weakness too. The demographic outlook is grim, threatening Germany's public finances. Education, once the envy of the world, is now mediocre—especially when it comes to universities, where the government is only just starting on reform (see article).

Admittedly, many other European countries have even bigger immediate problems than Germany. But the truth is that all of Europe needs reform: to shift away from high taxes, generous and wasteful welfare states, and, most of all, overly regulated and inflexible product and labour markets. If Mrs Merkel's Germany were to lead the way, it would be not just Europe's biggest economy but also its intellectual leader.

Smarter than Nicolas (let alone Silvio); but not Konrad

By that exalted measure, the CDU programme that Mrs Merkel will launch this weekend is likely to be disappointing. It will offer little more than promises of continuity, bolstered by the appeal of Mrs Merkel herself. That may be enough to win her re-election—Germans seem content with someone to reassure rather than inspire them. Yet Mrs Merkel ought to think about why she wants to be chancellor at all. If she does not set out plans for health-care reform, for more liberalisation of labour and product markets, for privatisation and for tax and spending cuts, she will have little chance of getting these through in office, whatever the make-up of her coalition.

Mrs Merkel will go down in history as Germany's first female leader—no mean feat. But if she wants to measure up to Adenauer or Helmut Kohl, she must persuade Germans of the case for change. And for that she needs to be far bolder.

Economist.com OPINION LEADERS

Iran's crisis

It is far from over

Jun 25th 2009
From The Economist print edition

Street anger may be fizzling, but infighting at the top could yet harm the regime more

AFP

AFTER just a week of heart-stirring popular defiance has Iran's new-found spirit of liberty already been broken? The demonstrations in the wake of what still seems to have been a fraudulent election victory for the country's gruesome incumbent president inspired awe; but as *The Economist* went to press their size appeared to have sharply dipped. The expression of dissent in rallies in a string of cities around the country seems to have subsided. It is still too soon to say whether some fresh incident may reignite mass anger in the near future, bringing millions back onto the streets, even forcing a rerun of the election. But the authorities, the security forces and their militia thugs, the *baseej*, sadly seem to have cracked enough heads to squash any immediate hope of setting aside a dodgy election, let alone ending rule by clerical fiat.

However, the courage of millions of ordinary Iranians will not have been in vain. The old establishment has not yet won and the crisis is far from over (see article). That is because the balance of power has shifted against the status quo.

Whatever the true result of the election, it is now plain that there is a vast constituency, even if it is not yet provably a majority, crying out for freedom. Mir Hosein Mousavi, the so-far-thwarted chief challenger to President Mahmoud Ahmadinejad, had been duly vetted by the clerical authorities as a proponent of their rule. But many of the millions who voted for him plainly hoped he would offer more freedom. As the old ruling circle has turned against him, even threatening him with imprisonment, he has boldly refused to bow out.

The legitimacy of the Islamic Republic has been spectacularly tarnished, both at home and abroad. Its claim to act as a beacon for Muslims, especially oppressed ones, in the region and around the world, has been ridiculed. Most dramatically, the position of the country's supreme leader, Ayatollah Ali Khamenei, has been sorely undermined. Once he posed as standing above the electoral fray, but he has now firmly come down on the side of repression and electoral fraud.

Perhaps the most damaging feature for the ruling clergy is the struggle that has broken out—for the first time so publicly—at the very top of the power structure. Forces loyal to Mr Khamenei and his bellicose president are now pitted openly against reformers and pragmatists backed by a former president, Akbar Hashemi Rafsanjani, hitherto considered Iran's second-most-powerful man, who, with another former president, Muhammad Khatami, a frustrated reformer, has outspokenly backed Mr Mousavi. So, even if the security forces manage to keep the dissenters off the streets, a bitter argument over the leadership of the ruling system will rage on. That battle may itself weaken if not topple the regime.

The world must watch and wait

Much as reform is to be desired, there is in truth little that outsiders can do to bolster the reformers. Barack Obama has rightly expressed greater outrage as the crisis has worsened. So have the leaders of Europe. But the American president has also been right to resist the temptation to call for the regime's downfall or take sides in the power struggle, let alone back Mr Mousavi for the presidency. That would play into the hands of those Iranians already trying to paint the challenger and his supporters as tools of the conspiratorial West. Plainly, business as usual cannot yet resume. But Mr Obama's prime aim is to persuade Iran to stop getting a nuclear weapon. To achieve that, he must still, sooner or later, seek to re-engage with Iran's government, whether it is led by a Holocaust-denier or a reforming Islamist who, when all is said and done, shares his rival's desire for Iran to obtain a nuclear capability.

Lord Elgin and the Parthenon marbles

Snatched from northern climes

Jun 25th 2009
From The Economist print edition

Greek demands to get back the Elgin marbles risk stopping a better idea: museums lending their treasures

AP

THERE is much to be said for moral clarity. Greece is insisting that the British Museum surrender the marble sculptures that Lord Elgin took down from the Parthenon and carted away in the early 1800s. Anything less, it says, would "condone the snatching of the marbles and the monument's carving-up 207 years ago." The Greek demand for ownership will arouse widespread sympathy, even among those who accept the British Museum's claim to the marbles. With the opening of an impressive new museum in Athens (see article), the sculptures from the Parthenon now have good cause to be reunited, if only for artistic reasons.

But sometimes clarity is self-defeating. A previous Greek administration was willing to finesse the question of ownership and co-operate with the British Museum over a joint display of the marbles. By hardening its position, the Greek government risks driving museums everywhere into clinging to their possessions for fear of losing them. If the aim is for the greatest number of people to see the greatest number of treasures, a better way must be found.

As curators all over the world will see it, those who call for the permanent return of the Parthenon sculptures from London are arguing for international museums to be emptied. Many other collections have a more dubious provenance than the marbles—think of the British Museum's Benin bronzes, seized in a punitive raid in Nigeria; of the Pergamon altar removed from Turkey and now in Berlin; of Chinese treasures carried off during the Boxer rebellion and again during the civil war; of hundreds of works in Russian museums that were snatched from their owners in the Bolshevik revolution.

You cannot go very far in righting those wrongs without entangling the world's museums in a Gordian knot of restitution claims. That is why, in December 2002, 18 of the world's leading directors—from the Louvre to the Hermitage and from the Metropolitan Museum to the Getty Museum—argued for a quid pro quo. The Munich declaration, as it is called, asserts that today's ethical standards cannot be applied to yesterday's acquisitions; but in return it acknowledges that encyclopedic museums have a special duty to put world culture on display.

This has led to a new level of co-operation between museums over training, curating, restoration and loans. Thousands of works are now lent each year between museums on every continent. Who thought that China's Palace Museum and the National Palace Museum in Taiwan would hold a joint show in Taipei, as they plan to in October, reuniting Qing-dynasty works that have been separated ever since they were borne away from Beijing by the retreating Nationalist forces in 1948? The British Museum was not party to the

Munich declaration, but it seems to embrace its spirit. During the Olympic games in China in 2008 it sent the Discobolus, the discus-thrower of Myron, to Shanghai where 5,000 people queued each day to see it. It will soon lend the Rosetta stone, the cornerstone of written language, to Egypt for the opening of the Giza museum. On the day the new Acropolis Museum was opened, the British Museum's director was in Riyadh, to arrange loans for an exhibition on the *haj* in London in 2011.

Beware of Greeks causing rifts

The choice is between the free circulation of treasures and a stand-off in which each museum grimly clings to what it claims to own. Instead of grandstanding, the Greek culture minister should call the British Museum's bluff and ask for a loan. The nervous British would then have to test the waters by, say, sending to Athens a single piece of the Parthenon frieze. If that piece were to be seized, then so be it. But if on the due date, the Greeks surprised everybody and returned the sculpture, then the lending programme would surely be expanded. By taking small steps, the Greeks may yet encourage the British to make the big leap.

Insider out

Jun 25th 2009
From The Economist print edition

Fusty old cliques v high-tech communities: it is a closer contest than you think

Illustration by David Simonds

RUMOUR has it that the former chief executive of one French corporate giant may have enjoyed only the appearance of being in charge. His talented number two was more senior in the hierarchy of the Masonic lodge to which both men belonged. Observers enjoyed speculating about which of them was really calling the shots.

Old-fashioned networks—alumni associations, social cliques and religious groups—continue to exert a surprisingly powerful influence on business around the world (see article). In French firms, where networks are particularly widespread, outsiders can find themselves struggling to navigate their way among the *énarques* and *polytechniciens* from the elite schools, not to mention all those masons.

Fortunately, digital technology appears to be thundering to the rescue of anyone blackballed by the old-style networks. For those denied entry even by the Benevolent and Protective Order of Elks, a declining American fraternal order, there is now a wide range of online business-networking sites. On LinkedIn, based in America, Xing, headquartered in Germany, or France's Viadeo, members can meet and keep track of dozens of contacts, with no need to perform strange rituals. Such sites transform every employee into an entrepreneur and facilitate all sorts of connections. Surely LinkedIn, which has members in over 200 countries, is likely to be a more fertile source of contacts than a college reunion dinner?

It is not hard to say which should be doing better. Old-fashioned networks do no good either to companies or to society. When jobs and deals go to the good old boys, networks tend to undermine meritocracy. They encourage bosses to recruit people like them. Being mostly male and white, cliques tend to encourage discrimination against women and ethnic minorities. Online networks, by contrast, make both companies and society work better. They create links that cross national borders. They help people to exchange information about each other's talents and businesses. They encourage the generation of new business ideas.

Conservation programme for Elks

To their supporters, the beauty of digital networks, unlike those snooty, exclusive old-fashioned networks, is they are inclusive. Anybody can belong to them. But that is their problem—or at least it is, once you look at it from the point of view of individuals rather than society as whole.

For better or worse, an Elk, an *énarque* or an Etonian knows something about his fellows, and those networks are small enough to encourage members into the exchange of favours, confident that they will be returned. Membership of LinkedIn conveys much less information to others, and the network may be too large and too fragile to encourage the exchange of favours. (It might be looked on more warmly if its members did not deluge people with invitations to join them.)

And for meritocrats it could get worse. In the future online networks may merely end up adding new power and scope to the old-fashioned sort. Elks can now seek out their deerest friends in metals trading or Mogadishu or any other corner of business far more easily than they could in the days when networks communicated through winks, nods and funny handshakes. More powerful cliques are now just a click away.

Ageing in the rich world

The end of retirement

Jun 25th 2009
From The Economist print edition

Demography means virtually all of us will have to work longer. That need not be a bad thing

Alamy

WHEN Otto von Bismarck introduced the first pension for workers over 70 in 1889, the life expectancy of a Prussian was 45. In 1908, when Lloyd George bullied through a payment of five shillings a week for poor men who had reached 70, Britons, especially poor ones, were lucky to survive much past 50. By 1935, when America set up its Social Security system, the official pension age was 65—three years beyond the lifespan of the typical American. State-sponsored retirement was designed to be a brief sunset to life, for a few hardy souls.

Now retirement is for everyone, and often as long as whole lives once were. In some European countries the average retirement lasts more than a quarter of a century. In America the official pension age is 66, but the average American retires at 64 and can then expect to live for another 16 years. Average spending on public pensions across the OECD is now the equivalent of more than 7% of GDP (they cost America just 0.2% back in 1935). In some countries the current figure could double by 2050, to say nothing of the cost of private pensions and extra spending on health and long-term care.

Grey and proud of it

Although the idea that "we are all getting older" is a truism, few governments, employers or individuals have yet come to terms with where longer retirement is heading: the end of the whole concept (see special report). Whether we like it or not, we are going back to the pre-Bismarckian world, where work had no formal stopping point. That reversion will not happen overnight, but preparations should start now—to ensure that when the inevitable happens it is a change for the better.

It should be for the better because it is being partly driven by a wonderful thing: people are living ever longer. Life expectancy has been rising by two or three years for every ten that pass, despite repeated forecasts that it was about to reach its limit. Centenarians used to be rarer than hens' teeth; now America alone has 100,000 of them. By the end of this century the age of 100 may have become the new three score and ten.

This imminent greying of society is compounded by two other demographic shifts. First, in most rich countries women no longer have enough babies to keep up the numbers (a prospect that may please a lot

of greens but not many governments); and the huge baby-boom generation, born after the second world war, has begun to retire. In 1950 the OECD countries had seven people aged 20-64 for every one of 65 and over. Now it is four to one—and on course to be two to one by 2050. That will ruin the pay-as-you-go state pension schemes that provide the bulk of retirement income in rich countries.

It is tempting to think that some of the gaps in the rich countries' labour forces could be filled by immigrants from poorer countries. They already account for much of what little population growth there is in the developed world. But once ageing gets properly under way, the shortfalls will become so large that the flow of immigrants would have to increase to many times what it is now. Given the political resistance to even today's levels of immigration (as shown up in the recent elections to the European Parliament), that, alas, looks unlikely.

So individuals, companies and governments in rich countries will have to adapt. There are some signs the first two are beginning to do that. Many employers remain prejudiced against older workers, and not always without reason: performance in manual jobs does drop off in middle age, and older people are often slower on the uptake and less comfortable with new technology. But people past retirement age would not necessarily carry on in the same jobs as before. In Japan, where pensions are Spartan and lots of people are still working in their later 60s and even 70s, big companies like Hitachi have found ways of re-employing staff after retirement—but in a different capacity and, significantly, at lower pay.

Elsewhere employers have been less inventive. But retailers such as Wal-Mart or Britain's B&Q, and caterers such as McDonald's, have started hiring pensioners because their customers find them friendlier and more helpful. And skills shortages are already creating opportunities: in the past year or two a dearth of German engineers has caused companies to bring back older workers. Once labour forces start declining, from about 2020, employers will no longer have much choice.

As for the older workers themselves, many of them seem keen enough to carry on beyond retirement. A recent *Financial Times*/Harris poll showed most Americans, Britons and Italians would work for longer in return for a larger pension (though Germans were much less enthusiastic). This surely makes sense: as long as the job is not too onerous, many people benefit in mind and body from having something to get them out of the house. Many baby-boomers say they never want to bow out altogether, though they would often prefer to put in shorter hours. If they want to go on working, they will have to accept that pay can go down as well as up.

It will all work out, sort of

Can governments make sure this inevitable adjustment goes smoothly? In the recent past some policies have bordered on the demographically insane—for instance "job-creation" schemes that encourage older workers to take early retirement. Many things that make sense anyway, such as making benefits more portable, encouraging immigration, promoting private saving or reforming health care (see article), make even more sense now. Banning mandatory retirement ages in the private sector (as America has done) looks sensible, as does creating conditions in which people can retire more gradually. Above all, the retirement ages for state pensions need to be put back. Recent increases to 67 or 68 are doing no more than compensate for the likely rise in life expectancy: 70 would be a better figure. So far only Denmark has taken the radical step of indexing the pensionable age to life expectancy.

Some of this will be unpopular. Private pensions, which might make up for some of this, last year lost nearly a quarter of their value, a terrifying $5.4 trillion. But as Herb Stein, an economist, pointed out, "if something cannot go on forever, it will stop." Better to try to enjoy the consequences.

On Silvio Berlusconi, malaria, European institutions, blue-collar workers, freedom of information, debt, financial expectations, emissions, Asia, Peter Mandelson

Jun 25th 2009
From The Economist print edition

Italy's prime minister

SIR – Your article on Silvio Berlusconi and the press stated that "Italy's prime minister campaigns against the foreign media", and supported this theory with a series of affirmations and allusions bereft of names and dates ("Language problems", June 20th). I would therefore like to specify that, first, an Italian newspaper, *La Repubblica*, wrote that "a foreign journalist in Rome was recently summoned to the foreign ministry." But the very same journalist, Philippe Ridet of *Le Monde*, immediately denied this and the author of the article admitted his error. To whom is *The Economist* referring? Second, Mr Berlusconi's staff have never tried to "get one foreign ambassador to bring journalists from his country into line". To which ambassador is *The Economist* referring?

Third, it is not true that Mr Berlusconi often sues newspapers. Since his third election as prime minister he has not sued any journalist.

And finally, the legal action regarding a number of photographs is aimed at protecting the privacy of Mr Berlusconi's guests and not his own. The right to privacy is guaranteed by the constitution.

Paolo Bonaiuti
Undersecretary of state and spokesman for the prime minister
Rome

Development experience

SIR – You seem to support research into "devising laser-defence systems to shoot down mosquitoes and prevent the spread of malaria" ("Zap!", June 6th). Lasers are not the solution to malaria. Indeed, I think many high-tech development solutions, like one laptop per child and Star Trek-style insect-blasting phasers, are a waste of time and money.

I worked for the volunteer Peace Corps in rural Zambia. The place where I lived had a well to provide clean water, but it sat idle because a simple five-cent plastic washer inside the pump was damaged and neither a replacement nor the tools to open the pump's housing were available.

My own hut had a sizeable gap between the mud-brick wall and the thatched-grass roof, numerous holes in the thatching and between the wooden door and the wall. I can't imagine what kind of laser system would have secured my hut against mosquitoes, much less who would have come to fix it when it failed. Were I still in Zambia I might have heard this story on the international news, except that the crank arm for charging my short-wave radio broke off and it never worked again. If there is an answer to malaria it is bednets and only bednets.

Zachary Wells
Monterey, California

David Beckham for president

*SIR – Charlemagne and politicians in the European Parliament are making exactly the same mistake, thinking that the lack of interest in the recent elections, or anything else related to the parliament, stems from the institutional structure and the powers it may or may not enjoy (June 13th). Rather, as in many

human matters, it is a problem of tribal identification or lack thereof. Note how much interest a completely trivial debate such as the outburst by Lord Rogers against Prince Charles can create, while a very important event such as elections to the European Parliament leaves just about everyone indifferent.

This is entirely due to the tribal nature of the human beast. Prince Charles occupies a totemic place in the tribal order, just as national parliaments do. From a tribal perspective, European institutions are completely invisible, except to the loony nationalist fringes.

Charlemagne is right to suggest that we stop tweaking the institutions to make them relevant, but wrong in thinking the answer is to repatriate powers to the national governments. The right approach would be for the European institutions to learn to communicate on the tribal level.

David and Victoria Beckham for European presidents, is one thought. Or how about offering a completely powerless European tsardom to some otherwise redundant minor member of the Romanov family? What the European Union needs are some human faces and a few sexy titles to make it all seem real. Sorry, José Manuel Barroso won't cut it until he turns himself into BarroStarDust.

Michael Eustace Erwin
Paris

Job insecurities

SIR – Lexington tried to find some reassurances for blue-collar workers, who are dropping out of the affluent middle class in large numbers (June 6th). He concluded that "there is still hope for blue-collar workers…willing to learn from the calamity that is General Motors". However, even rueful and sobered workers cannot create jobs: that is mainly the function of investors, who usually want to cut wages and benefits. In the longer run virtually all manufacturing faces an equalisation of factor prices due to the globalisation of trade, a process that will keep pushing American prices and wages well below our current middle-class levels.

Edwin Reubens
Emeritus professor of economics
City University of New York
Weston, Florida

SIR – The 1950s and 1960s were the high-water mark for the American worker. All Americans prospered because ours was a domestic economy. The American government was allied with business, as it has always been, but the interests of business and its workers were complementary. What has changed is that these interests are no longer the same. Workers are still national but business is now global. Theorists speculate about the elimination of the nation state in favour of some kind of global trade enforcement. Yet workers continue to believe that their government should work for them. Protectionism could offer the American worker a much less negative outcome than the one he is currently facing.

Lee Tallman
Peoria, Illinois

The right to know

*SIR – Freedom of information in Britain will only become a reality, as you suggest, when the delays that bedevil the appeals system are reduced to months, not years ("Uncovering the next scandal", June 6th). My research into the workings of the 2000 act revealed that 75% of appeals to the information commissioner related to refusals by government departments. There is clear evidence that delays at the commissioner's office and time taken for appeals at the information tribunal are exploited by officials to manage possibly embarrassing disclosures so that their news value is reduced.

Journalists' inquiries into the Formula One tobacco-sponsorship ban and Bernie Ecclestone's meeting with Tony Blair when he was prime minister, to take one example, were only accommodated after Mr Blair left office.

Providing extra funds to the commissioner's office to deal with delays will only free up freedom of information if its caseload does not continue to grow. Bringing in private companies working in the public sector under the aegis of the act, while a demonstration of good faith, is likely to bring the system to a near halt.

Jeremy Hayes
BBC Radio 4
London

Economic frame of reference

SIR – I was struck by your leader on debt, not so much for its conclusions, but by its language ("The biggest bill in history", June 13th). You used the adjective "rich" no less than seven times to describe countries that now stagger under a monumental weight of indebtedness. By the same token, the adjective "emerging", when used with reference to developing nations, seems almost pejorative, given that so many of these countries now have better prospects for economic growth: zestier demographics, larger foreign reserves, dramatically reduced sovereign-debts, stabler banking systems, and superior household finances and savings rates.

Could there be a more accurate way to describe the supposedly rich economies? If not "poor", then how about "grievously indebted"?

Tim Price
Director of investment
PFP Wealth Management
London

Expectflations

*SIR – I noticed your chart on falling stockmarkets (Economic and financial indicators, June 13th). Yet investors continue to be optimistic despite the continuing stream of grim economic data (the number of American mortgages still in arrears, Chinese exports falling precipitously, etc). We need a new term for finance—expectflation: (noun) the unrealistic inflation of expectations, such as "the markets hit a new high today, but analysts continue to speculate whether this is really based on fundamentals, or just expectflation".

Ben Cijffers
Kuala Lumpur

Taxing emissions

*SIR – Congratulations for "continuously advocating a tax on carbon", to the point that spokesmen for Duke Energy and the International Emissions Trading Association (IETA) felt they had to reply (Letters, June 13th). The Duke spokesman said the bill in Congress "distributes a substantial portion of emission allowances to regulated, local distribution companies and helps to protect electricity customers from unnecessary price rises". But if the legislation succeeds in reducing emissions, the reduced supply of electricity will necessitate a rise in retail prices to reduce demand for the reduced supply. This consumer-price rise is independent of how much or whether the power company paid anything for its emission permits. Giving the permits away free will affect the profits of Duke Energy, not the retail price of electricity.

The IETA spokesman argued that "well-designed markets will promote rational 'buy-versus-build' decisions". No: it is predictable and stable prices that will do this. A tax is better able to provide predictable prices than any amount of trading. A tax would allow us to dispense with the whole secondary and derivatives market that is a deadweight loss to consumers, and the whole reason for IETA's existence.

The Waxman-Markey bill is a 932-page monstrosity and full of pork. Much better 20-page bills, such as Chris van Hollen's tax and dividend, were under consideration.

Wilfred Candler
Annapolis, Maryland

Asia's naval powers

SIR – I disagree with Banyan's assertion that Asia's rising powers are "chasing ghosts" when it comes to maritime security (June 13th). Banyan referred to Alfred Thayer Mahan, "the founding father of geopolitics", who thought that sea power played a decisive role in national security and economic development. The British decision in the 17th century to establish a permanent, standing fleet, for example, was based on a hard headed calculation of national interest rather than any perception of the intrinsic worth of a navy. Hitherto, English naval power was primarily about transporting troops. Control of the sea surrounding the British Isles was relatively neglected, attested to by the frequency with which foreign governments and rogue political elements could project power from Europe onto the British mainland.

Most crucially, Mahan argued that the grand strategy of states like Britain was shaped by the maritime environment, requiring a capable fleet to protect sea lanes and thrust might overseas.

Rapidly developing countries such as India and China rely on secure sea lanes to transport manufactured goods and import food and raw materials. The maritime state that neglects its navy is one that finds itself unable to preserve its sovereignty. It is this harsh realpolitik calculation about security and the maintenance of state sovereignty that shapes Chinese, Indian, Japanese or indeed Malaysian policy.

Justin Boston
Fareham, Hampshire

Mandy plays ball

SIR – Bagehot compared Lord Mandelson's unhappy alliance with Gordon Brown to the handling of that "completely New Labour dog", Fitz (June 13th). The resemblance to the "truculent" bulldog that appeared in Labour's 1997 campaign goes further than that. During the campaign, a poster featuring Fitz was delicately retouched, apparently on the instructions of Peter Mandelson, in order to airbrush out the dog's testicles. It would seem that Peter's pets are rather prone to emasculation, by one means or another.

Tim Johnson
London

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*Letter appears online only

Germany's chancellor

Merkel is the message

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From The Economist print edition

No other German politician comes close to matching her popularity. How does she do it? And what does her ascendancy say about her country?

AP

WHAT oratory is to Barack Obama, the photo-opportunity is to Angela Merkel. In a red parka before a receding iceberg in Greenland; among dark-suited world leaders, one of them yet distinctive in her signature trouser-suit; sombre in black alongside Mr Obama at the Buchenwald memorial site. Through such images, the chancellor has defined herself in the eyes of her fellow Germans as a leader who holds her own in the highest councils and masters the knottiest problems. On June 25th and 26th, as *The Economist* went to press, Ms Merkel was scheduled to visit Mr Obama in Washington, which will no doubt produce another flattering harvest.

This will matter in the federal election three months later. On September 27th Ms Merkel's Christian Democratic Union (CDU) will face off against the Social Democratic Party (SPD), currently its reluctant partner in Germany's "grand coalition" government. Each hopes to jettison the other and form a coalition with a like-minded smaller partner. Frank-Walter Steinmeier, the SPD foreign minister, aspires to lead a coalition with the Greens (and, if necessary, the liberal Free Democratic Party, or FDP). The conservative CDU prefers to govern with the liberals alone. Along with its Bavarian sister party, the Christian Social Union (CSU), it will publish its campaign platform on June 29th. But the CDU's trump card is Ms Merkel herself. Supporters wear orange T-shirts with the legend "teAM Deutschland", exploiting her initials. She is the clear front-runner, and may yet succeed in forming a "bourgeois" coalition with the FDP.

On several counts, that result would be surprising. Germany's export-dependent economy, the world's fourth-largest, will contract by 6.1% this year compared with a 4.8% drop in the Eurozone overall, according to the OECD. Abroad, Ms Merkel has been blasted for doing too little about that. Germany does not comprehend the "importance of fiscal mobilisation" (ie, it is not spending enough), complained Japan's prime minister, Taro Aso, before a crisis summit in April. Perhaps that is because Ms Merkel herself "does not seem to understand the basics of economic policy", speculated Adam Posen of the Peterson Institute for International Economics in Washington. Mr Obama will no doubt be more polite, but he is likely to press Ms Merkel to do more in Afghanistan and to accept prisoners from Guantánamo Bay.

What foreigners denounce as cluelessness Germans see as cool-headedness. Nearly 60% are satisfied with the grand coalition, according to a recent poll by Forschungsgruppe Wahlen; 78% think Ms Merkel has done well as chancellor and 58% want her to remain in the job. Change, if it happens, is unlikely to be the sort one expects during a crisis of capitalism. The most probable alternative to the status quo is a coalition with

the business-friendly FDP, which favours lower taxes, freer markets and more limited government.

Events could upset this placid scenario. Exporters and their suppliers will eventually be forced to sack workers on a large scale. By the end of 2010, predicts the OECD, the number of unemployed will rise to 5.1m from last year's average of 3.3m. On election day voters could already be in a vengeful mood. But time is running out for the chancellor's foes. Ms Merkel, who took up politics at the advanced age of 35, is likely to govern Germany for the next four years.

A woman of mystery

Though she has been in office nearly that long, she remains a puzzle. Germans find it easier to say what she is not than what she is. She is certainly not a towering chancellor in the mould of Konrad Adenauer or Helmut Kohl. "Iron lady" does not fit. Nor is she a great communicator. Pundits plead for a blood-sweat-and-tears speech on the economic crisis, but she has yet to deliver it. She does not exude maternal warmth. Ideology is not her strong point.

Her offbeat biography adds to the difficulty of pinning her down. Her election in 2005 as Germany's first female chancellor and the first from the ex-communist east had Obama-esque novelty. The daughter of a Protestant pastor who migrated east, she leads a party whose core is Catholic and whose roots are in western Germany. The fall of the Berlin Wall drew her into politics and Mr Kohl propelled her towards the top, naming her minister for women and youth in his third cabinet. Physics preceded politics in her career; its analytical habits still shape her style of governing. And yet Ms Merkel, who has been spotted doing her own shopping, connects with voters. People think of her as "the matriarch who takes care of them," says Manfred Güllner of Forsa, a polling firm. Without charisma, she contrives to shine.

She starts the electoral season with a hoard of political capital. The football World Cup, hosted by Germany in the summer of 2006, seven months after she took office, bathed the country and the chancellor in laid-back patriotism. In 2007 Germany assumed the rotating presidency of the European Union (for six months) and presided over the G8 summit of the world's biggest economies, allowing Ms Merkel to display a flair for statesmanship. For nearly three years the economy was benign. Buoyed by world trade, economic growth averaged 2.3% from 2006 to 2008, the highest rate this decade. Unemployment fell from nearly 5m in 2005 to around 3m. Before the crisis the federal government was within sight of its cherished goal of balancing its budget by 2011.

The gravest charge against Ms Merkel is that she amassed too much political capital and spent too little. She campaigned for the chancellorship (and nearly lost) as a determined reformer who would unshackle enterprise, unburden taxpayers and " govern through" all obstacles. The tax code should be simple enough to fit on a beer mat, her party declared. But she quickly adapted to the constraints of the grand coalition, forced upon her by the CDU's narrow victory. She stands accused of governing less as a leader than as a moderator, brokering compromises among the coalition's warring factions and then claiming credit for whatever emerges.

To many, the results have been disappointing. The SPD entered the grand coalition with an acute case of reformers' remorse. Under Ms Merkel's predecessor, Gerhard Schröder, the SPD and its Green allies enacted necessary but unpopular changes to welfare and labour markets collectively known as Agenda 2010, which nearly tore the SPD apart. Demoted to junior status in Ms Merkel's government, it had no desire to repeat the experience. Despite majorities (at first) in both houses of the legislature, the grand coalition passed just one big-ticket reform in the spirit of Agenda 2010, a gradual rise in the retirement age to 67.

More often, with Ms Merkel's help, it rolled back reform. It lengthened the time for paying unemployment benefits to older workers, offered pensioners relief from rising prices and introduced minimum wages in half a dozen industries, including postal and security services.

Sitting out trouble

Despite the incessant deal-making, much of Berlin's political class is feeling sour. The SPD resents Ms Merkel for stealing its clothes. The CDU's "economic wing" thinks she has pandered too much to the SPD. The CSU, struggling to stay on top in Bavaria, defies the chancellor on taxes, health policy and anything else it thinks will pacify touchy constituents. Tensions over policy have grown with the sinking of the world

economy. Liberals who saw an ally in her feel let down. Ms Merkel “has not said a dumb sentence in three-and-a-half years,” says Michael Eilfort of the Market Economy Foundation in Berlin. “But there seems to be no theme for which she has an enduring passion.”

A reputation for wishy-washiness could cause problems. Mr Steinmeier has begun to hammer away at her leadership style, which he describes as “wait, watch, then jump on the bandwagon”. Germany’s consensus system of governance makes it difficult for any chancellor to impose his or her will, but Ms Merkel seems particularly disinclined. She learnt from Mr Kohl to “sit problems out”, says Gerd Langguth, a political scientist who has written her biography. Unlike her mentor, though, she has “no sense of historical mission” and “no vision of society”. Rather, she is a thoroughgoing pragmatist who “wants to solve today’s problems in such a way that she remains in power.”

Yet Ms Merkel has two traits that partly absolve her of the charge of being a soulless pragmatist. The first is what Mr Langguth calls her “fixed points”, most of which are connected to Germany’s relations with the rest of the world. Like many central Europeans liberated from communism, she is instinctively pro-American and warier of Russia than many mainstream German politicians (though American banks and Russian gas have tempered both instincts). She has rebuked the main powers for abusing human rights, receiving the Dalai Lama at the chancellery and calling on the United States to close Guantánamo. She can be counted on to resist attempts by fellow leaders, such as France’s Nicolas Sarkozy, to split the 27-member European Union into separate clubs.

Though an easterner, Ms Merkel has embraced the western German sense of responsibility for the Holocaust and is a staunch backer of Israel. Recently she upbraided the pope for re-admitting to the Catholic fold a Holocaust-denying bishop. This offended the CDU’s base of conservative Catholics, who have trouble enough relating to a divorced-and-remarried, childless, Protestant career woman from the east. Where Mr Kohl was “married” to the party Ms Merkel is merely “allied” to it, says Mr Langguth. But she is indispensable: with the backing of 35% of the electorate, the CDU is far less popular than she is.

Eyes on the future

Nor is Ms Merkel without vision. It is trained on the distant future, in particular on two issues whose consequences will be felt after her political career is over: climate change and demographic decline. As environment minister in the mid-1990s she helped negotiate the Kyoto protocol to reduce emissions of greenhouse gases. At her prompting, the EU committed itself to cutting emissions by 20% by 2020 (more if other developed countries agree to do so) and to supplying 20% of its energy from renewable sources by the same year. Germany is to be a model. Its own climate package mandates, among other things, a 30% improvement in buildings’ energy efficiency. The national goal is to cut emissions 40% by the 2020 deadline.

The second worry that underlies Ms Merkel’s policies is population decline. Within 30 years the proportion of Germans older than 65 will rise from a fifth to a third, and the population will shrink by a tenth. The younger generation will look different. In big cities today nearly half the children under 15 are immigrants or their children and grandchildren. In general, they are poorer, worse educated and more likely to be unemployed than non-immigrants. Germany needs more workers and better brains.

Ms Merkel has made a start. She appointed as family minister a glamorous mother of seven, Ursula von der Leyen, who introduced “parents’ pay”, a 14-month stipend for parents of newborn children linked to their salaries, encouraging middle-class women especially to combine family and career. To bolster the woefully underdeveloped day-care system, a new law promises to provide enough places for 35% of children aged three or less by 2013.

Ms Merkel’s campaign to turn Germany into an “education republic” has made less progress, partly because primary and secondary education is the province of the states. But her government recently approved €18 billion ($25 billion) of extra funding for research and universities, a noteworthy promise at a time of spiralling debt (see article). It produced a €750m “national integration plan” to promote jobs and education for minorities, for example by expanding compulsory German-language and culture courses.

Mrs von der Leyen says her boss has modernised her traditionalist party as well as the country. Thanks to her, “We’ve gone from saying ‘We’re not an immigration country’ to accepting that we are one.” In the CDU day care is “no longer a taboo. Without Ms Merkel that would have been unthinkable,” she says. The chancellor sees herself, one suspects, as a latter-day *philosophe*, who seeks cures for society’s ills in reason and science.

Balancing the bail-outs

Her achievements in such areas lag behind her ambitions. Universities remain under-funded. Integration has progressed slowly. The government offended Turks by changing the immigration law to require migrants from poor countries to pass a language test before joining their spouses in Germany. Last year the number of immigrants obtaining German citizenship fell to its lowest level since unification. When far-sightedness crumples into ordinary opportunism, Ms Merkel disappoints. Saying climate protection cannot come at the expense of German jobs, she pushed for looser emissions standards for carmakers, putting the EU’s overall emissions targets in jeopardy, says Jeroen Verhoeven of Friends of the Earth in Brussels. To Hans Joachim Schellnhuber, head of the Potsdam Institute for Climate Impact Research, who advises her on climate issues, these are merely tactical compromises. Though willing to take detours, Ms Merkel “never loses sight of where she wants to go.”

If she wins re-election, she will have a chance to prove him right. But first she must ensure that voters do not punish her for a recession that is striking Germany with particular force. It helps that most see the downturn as a shoddy American import and have yet to feel its full impact. Credit and blame must also be shared with the SPD. Yet Ms Merkel knows that crisis management is ultimately her responsibility; if it is seen to fail she is likely to as well.

Reuters

Her party’s star

In some ways, her task is more difficult than Mr Obama’s or Mr Sarkozy’s. The economic slump is frightening, but to Germans the threats of inflation and ballooning government debt seem hardly less so. For Ms Merkel this means that over-reacting to the crisis is as much a danger as under-reacting. She thinks her government has struck a balance with three sorts of bail-out: of banks, of non-bank enterprises and of the economy as a whole. But in each case she risks getting the balance wrong.

That is especially true for banks. Ms Merkel and the finance minister, Peer Steinbrück, niftily headed off a banking panic last October by guaranteeing depositors' savings and rushing a €500 billion banking rescue through the Bundestag. But their proposals to shift banks' bad assets into "bad banks" would oblige them to pay off the losses over 20 years. That will make it hard for them to become good banks capable of attracting fresh capital.

A pair of stimulus packages worth €64 billion this year and next includes tax cuts, subsidies to keep workers in their jobs and a wildly popular €2,500 "bonus" paid to drivers who scrap old cars and buy new ones. Germans insist this is plenty. Tax cuts and extra spending add up to 1.6% of GDP this year and 2% in 2010, reckons the IMF, not counting automatic stabilisers such as unemployment insurance. But some trading partners still think Germany could do more, given its huge current-account surplus and its (pre-crisis) balanced budget.

Within Germany the big wedge issue has been rescues of non-financial enterprises. A €115 billion "Germany fund" provides guarantees and credits to companies that are in trouble through no fault of their own. Mr Steinmeier has vowed to "fight for every job", backed by CDU premiers when the jobs in question are in their states. Other conservatives fret that the government is throwing taxpayers' money away. Ms Merkel opted for a typical middle course, saying yes to a bail-out of Opel, the European arm of America's bankrupt General Motors, but no to Arcandor, a department-store group.

Messy, hesitant and opportunistic though the triple bail-out may be, it has not yet harmed Ms Merkel's standing with the voters. They continue to see her caution as wisdom, her penchant for splitting the difference as discernment. In resisting foreign demands to do more she is seen as standing up for German interests. If she did that stridently, Germans would be uneasy; perhaps because she is a woman, the perception is she does not. The moderating style that Mr Steinmeier sneers at is read by voters as a sensible reluctance to polarise.

In the early days of the recession, there were fears that Germans would react by rejecting their leaders and, indeed, the economic system that produced it. But it turns out that they are not keen to experiment in troubled times. Ms Merkel has encouraged that response by doing enough so far to contain the crisis while reaffirming bedrock German principles, such as the social-market economy. Germans trust the canny physicist from the east. Now she means to press that advantage home.

The recession and pay

The quiet Americans

Jun 25th 2009 | WASHINGTON, DC
From The Economist print edition

Employees are proving stoical in the face of pay cuts and compulsory unpaid leave

Illustration by David Simonds

BACK when times were better and the newspaper industry wasn't fighting for dear life, reporters at the Cleveland *Plain Dealer* would regularly grumble at the measly pay increases their union negotiated. Last month, when the union announced it had negotiated a 12% pay cut in exchange for a promise of no lay-offs, there was applause. "It took me aback," says Harlan Spector, a medical reporter and one of the negotiators.

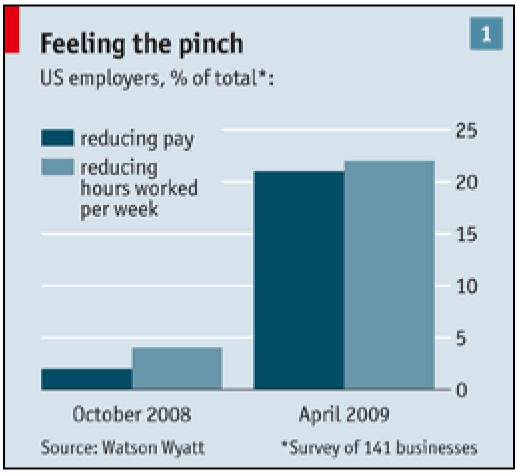
Like many long-standing economic relationships, "wage stickiness" is being tested by the savagery of the recession. Ordinarily, when unemployment shoots up wages do not tend to fall: they simply grow more slowly. Why the price of labour responds less to demand than that of other commodities is a bit of a puzzle. In the 1990s Truman Bewley of Yale University interviewed hundreds of employers and discovered that, faced with a slump in demand, they would rather lay some workers off than cut the pay or hours of everybody. The sackings devastated those directly affected, but broad cuts to pay and hours hurt everybody's morale. "The main drawback of pay cuts is that they fill the air with disappointment and an impression of breach of promise, which dissolve the glue holding the organisation together," he wrote in 1997.

In this recession hard-pressed employers are not just laying off workers but cutting wages and implementing "furloughs"—unpaid, compulsory time off. A survey by YouGov for *The Economist* this week found 5% of respondents had taken a furlough this year and 13% had taken a pay cut. Watson Wyatt Worldwide, a human-resources consultancy, says the proportion of American employers implementing either wage cuts or furloughs has risen sharply since October (see chart 1). Since September, as unemployment has jumped three percentage points, the average work week has shrunk (see chart 2) and hourly wage growth has slowed sharply to 3.1%. The slowing will be even sharper once a big fall in bonuses, especially in the finance industry, is included.

Higher inflation in the early 1980s and 1990s meant employers could simply freeze wages or raise them more slowly than prices to achieve real cuts in pay. This still dented employees' standard of living but without the humiliation of a smaller paycheck. Now

inflation is lower (in fact, negative because of a big drop in fuel costs). So, in the absence of big increases in productivity, wage cuts may be less avoidable. With households carrying big debts, falling incomes could heighten financial stress and, at worst, initiate a cycle of wage and price deflation.

Mr Bewley also found that psychological resistance to pay cuts melts when the employer's survival is at stake. In January 40,000 members of the Teamsters Union agreed to a 10% cut by YRC Worldwide, a trucking company, which is at risk of bankruptcy. "The company needs some help," a Teamster official said at the time.



Newspapers are also under severe pressure. The *New York Times* recently cut salaries temporarily by 5% in exchange for 10 additional days of leave. On June 23rd it reached an agreement with a union representing employees of the *Boston Globe* on a 6% pay cut. Employees had earlier voted against an 8% pay cut, but gave in when the *Times* threatened a 23% cut.

When the *Plain Dealer* first said this year it needed to reduce its labour costs by $5m, the newsroom was furious. For years the journalists had got by with wage increases of barely 1%, after higher health-care and pension contributions were subtracted. But the wave of closures and lay-offs throughout the industry was sobering. Last year 27 newsroom employees were laid off and only two have since found full-time work. "People are a little pale thinking about how to make their personal finances work [but] …we are ahead of what we were earning if we all had to find new work," says Karen Long, the books editor and a union negotiator. The 12% pay cut consists of an 8% cut in pay rates plus 11 furlough days. If the company lays anyone off after the one-year agreement, pay automatically jumps back to its previous level.

In a society known for competitive individualism, pay cuts and furloughs are calling forth a spirit of collectivism. Hewlett-Packard, Advanced Micro Devices and FedEx have trimmed rank-and-file pay, but their chief executives have taken 20% pay cuts, says Challenger, Gray and Christmas, an outplacement consultancy. Slumping tax collections forced city administrators in Lima, Ohio, to draw up contingencies for a 10% cut in hours for all but emergency workers. But first the city's eight most senior administrators gave up a 2.5% pay rise.

All together, for the moment

Not all such negotiations are being welcomed, however. In California home-care workers, who look after the infirm in their own houses, have demonstrated against Governor Arnold Schwarzenegger's proposal to cut their pay to the state minimum wage of $8 per hour. Their pay has already been reduced to $9.50 an hour from between $10 and $12 according to UDW Home Care Providers Union, one of their unions. To take another example: when the restaurant where Sandy Jaffe is a waitress near Los Angeles cut everyone's hours in half because of slumping business, she was annoyed management didn't trim the hours of less productive staff more.

Still, most Americans seem to be responding stoically. Signs that the recession is bottoming out means the pressure for more cuts is ebbing: this week, a report from the OECD suggested that growth in the rich countries could resume next year, albeit at an anaemic 0.7%.

Although no one is happy to have their pay cut, many seem to like a brief break from the rat race. Some employers forbid employees to do anything even work related on their furloughs, such as checking

voicemail or BlackBerrys. In some circumstances that could require the employer to pay the employee for the whole week.

When the teachers' pension plan that Susan Daniel works for in California decided to furlough employees for two days each month, she welcomed the chance to spend the days at home with her husband and to get around to rebuilding the backyard deck. To cut costs, she gave up bottled water and her cable-TV service. The fact that everyone, including her boss, is getting the same treatment makes it much more bearable. “At least we have our jobs and our benefits,” she says.

Welfare claims surge

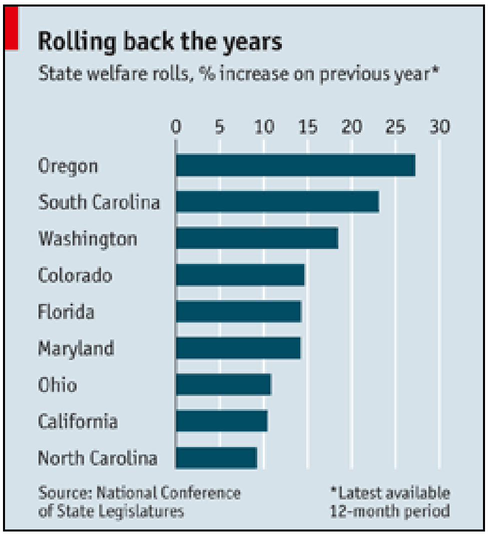
Helping the needy

Jun 25th 2009 | GLEN BURNIE, MARYLAND
From The Economist print edition

Or reform going into reverse?

LUNCH is a ladle of chilli with rice, cornbread, salad and a slab of chocolate cake. The Seventh-Day Adventist soup kitchen in Glen Burnie, Maryland, serves a hot meal each Tuesday to anyone who shows up. Families can take home monthly bags of extra food and second-hand clothes, too.

It's busy. Carolyn Goss, the manager, reckons that half of the 150 people she feeds each week have fallen on hard times only recently. As the recession rumbles on, the number of Americans claiming welfare (cash assistance aimed mostly at poor mothers of dependent children) appears at last to be rising. A survey by the National Conference of State Legislatures found increases in 23 of the 30 largest states in the past year. The welfare caseload rose by more than 20% in Oregon and South Carolina, and by more than 10% in California, Colorado, Florida, Maryland, Ohio and Washington state. This is the first time since the big welfare reforms of the 1990s that the total number of recipients has increased. (The national caseload fell from 4.5m in 1996 to 1.6m last year. This year's national figures are not yet available.)



Some see surging caseloads as evidence that the safety net is working. When times are tough, extra payouts cushion the pain. Doomsayers on the left, who predicted calamity when welfare was made temporary and conditional on seeking work, have been proved wrong, says Ron Haskins, an architect of welfare reform now at the Brookings Institution, a non-partisan think-tank.

But others fret that the work of welfare reform is being gradually undone. This year's stimulus bill provides extra cash for states whose welfare caseloads increase. This gives them an incentive to enroll more people, says Katherine Bradley of the Heritage Foundation, a conservative think-tank. Congress also reduced the proportion of welfare recipients who must find work if a state is not to lose subsidies. Ms Bradley predicts that states will respond by relaxing work requirements. Mr Haskins thinks not. Most states are keen to get as many people working as possible, he reckons, though the recession makes this hard.

It will be a while before anyone knows who is right. America's safety net is multilayered and varies from state to state. When workers are laid off, they often receive lump-sum severance payments. Next comes unemployment insurance, which used to last only for six months but which Congress keeps extending. Hard-up families can also apply for food stamps, which are relatively easy to claim. The number of Americans receiving them has risen sharply, from 24.9m in September 2007 to 33.2m in March this year.

Welfare is harder to claim, so the numbers getting it have risen more slowly. Another factor is that most welfare claimants are women, whereas most of those laid off in the past two years have been men. Thousands of hard-hat jobs in construction and manufacturing have vanished, while female-dominated sectors such as health-care and education are hiring more hands. Male unemployment is 10.5%; for women it is a somewhat less dismal 8%.

An unscientific poll of soup-kitchen clients in Glen Burnie suggests that the able-bodied jobless are getting by on a mixture of public assistance and private charity, but still have plenty of incentive to find work. Ernest Bedford, for example, is down to his last $15, having been laid off as a bus driver. He trekked 1,400 miles (2,200 km) to Texas to find a job as a truck driver, but failed to get it and came home. Undaunted, he has been searching for work online, using the free computers at a public library. He hears they need drivers at Baltimore airport. He says he expects to have a job by the end of the week.

The Voting Rights Act

Sacred, or outdated

Jun 25th 2009 | WASHINGTON, DC
From The Economist print edition

The Supreme Court opens the door for updated racial voting laws

Corbis

A long time coming

IT IS one of America's greatest laws, and one of the least understood. The Voting Rights Act of 1965 forced Southern states to let black Americans vote. In theory, they already had that right, but Southern whites found ways to prevent them from exercising it, such as impossible-to-pass "literacy" tests, selectively applied. The act banned all such tricks, thus removing a terrible stain on American democracy and paving the way, four decades later, for the election of the nation's first black president.

Yet parts of the act are still subject to legal challenge. Given its iconic status, many Americans find this confusing. Some even imagine that the act itself is in peril, which it is not. But one of its provisions could be on borrowed time, judging by the subtext of a Supreme Court ruling this week.

It was clear, when the act was passed, that Southern whites would try to subvert it. So Congress included a temporary emergency provision, Section 5, requiring districts with a history of discrimination to win approval from the federal Justice Department before changing even the smallest electoral rule, such as moving a polling station. Section 5 was supposed to last until 1970. But Congress keeps extending it, and it is now scheduled to expire in 2031.

Critics raise two objections. Draconian federal control of local electoral rules was justified in 1965, they say, but not now. Also, the Voting Rights Act has been interpreted to require states to cobble together majority-black voting districts wherever possible. The assumption is that whites will not vote for blacks. But this is hardly an iron rule: Barack Obama won a bigger share of the white vote than John Kerry or Al Gore.

Against this backdrop, a Texan utility district (an area where the provision of services is administered by an elected board) with no history of racial discrimination asked to be released from Section 5's strictures. A lower court said no. But by an 8-1 majority, the Supreme Court overturned its ruling on June 22nd. It did so on narrow technical grounds. But it left wide open the possibility that a future, broader challenge might succeed. Section 5 "raises serious constitutional concerns", wrote Chief Justice John Roberts. Federal intrusion must be justified by "current needs" he said, not historical ones.

Some civil-rights groups argue that without a federal leash, Southern racists would quickly deny the vote to many blacks. "Jim Crow might be dead but James Crow Esquire is alive and well, and while we may not see fire hoses and police dogs any longer, they have been replaced by false e-mails and polling station trickery," says Benjamin Jealous, the head of the National Association for the Advancement of Coloured People.

Abigail Thernstrom, the author of "Voting Rights—and Wrongs", disagrees. She argues, counterintuitively, that racial gerrymandering reduces black political influence. Majority-black districts tend to elect politicians who appeal to black solidarity but do not need to woo whites. Moderates do less well: Mr Obama was thrashed by 30 percentage points when he ran for Congress in a majority-black district. The net effect of cramming blacks into racially homogenous districts is that the congressional black caucus, with some exceptions, clusters at the fringe of American politics, rather than at the centre, where decisions are made. Segregated voting districts thus impede political integration, says Ms Thernstrom.

Captain America

He's back

Jun 25th 2009
From The Economist print edition

Just in time for the 4th of July

AP

CAPTAIN AMERICA was an immediate success in his first appearance on the eve of America's entry into the second world war. Too frail for military service, art student Steve Rogers volunteered for an experiment to create an army of super-soldiers. After being both injected with a serum and exposed to radiation, Rogers achieved human perfection. Armed only with an indestructible shield presented to him by Franklin Roosevelt, the Captain made war on the Axis. The cover of his first comic book, which hit the news-stands a year before Pearl Harbour, showed him punching Hitler in the face.

Captain America faded after the war and, after a brief revival to fight the communists, disappeared until he was unfrozen from a block of ice in 1964. Though the embodiment of patriotism, he was no right-winger. During the Vietnam war he stayed at home. He teamed up with the Falcon, the first African-American superhero. During Watergate, he discovered a fascist conspiracy at the heart of government, and was so disillusioned that he briefly became a stateless hero called Nomad.

In his long-running battles with the Nazi villain Red Skull and the Swiss anarchist Flag-Smasher, among others, the Captain fought with the trademark Marvel Comics blend of fantasy and all too human failing. His most recent death, two years ago, was part of an involved story about a government effort requiring superheroes to register, which he fought in court. Now Marvel is to bring him back on July 1st.

Captain America's film is set for release in 2011, following in the footsteps of Spider-Man and Iron Man. Set again in the second world war, it will test whether a 21st-century audience can embrace the heroics of a simpler time.

Cleaning the Great Lakes

Swimming with E. coli

Jun 25th 2009 | PORTAGE, INDIANA
From The Economist print edition

New efforts to reverse centuries of abuse

IT IS high season for a sliver of sand in Portage, Indiana. A pretty visitors' centre sells ice cream. Lake Michigan shimmers in the sun. And beside the beach is a roaring steel mill. Swimmers enter the water at their own risk.

The Great Lakes—Michigan, Huron, Erie, Ontario and Longfellow's "shining Big-Sea-Water", Lake Superior—comprise one-fifth of the world's surface fresh water. They have also endured centuries of abuse. But advocates are cheerful these days. Barack Obama's budget proposes $475m for restoration. In June he appointed a Great Lakes tsar, Cameron Davis, to begin work in July. There is much to do.

Exploitation began in the 17th century. In 1634 a Frenchman arrived on a lake's shore wearing a mandarin robe, hoping to find Cathay. He found Wisconsin. Despite such disappointments, the lakes drove fast growth. They sped the shipment of furs, then timber, iron, grain and coal. For decades industrial plants have lined the shores, using water as a coolant. All this activity has taken a toll: 40 years ago this month the Cuyahoga river, which empties into Lake Erie, caught fire.

The 1970s brought reform, such as the Great Lakes Water Quality Agreement that sought to restore the lakes' "chemical, physical and biological integrity". But problems remain. Sewage systems continue to overflow, forcing many beaches to close. Levels of some toxins in fish have declined, but others pose new risks. Atlantic freighters still bring in foreign species—there are now 185. Regulations are tangled. In 2007 a refinery in Indiana received a permit to increase discharges into Lake Michigan. Only public uproar prevented it.

Better co-ordination would help. The Great Lakes region includes two Canadian provinces (Ontario and Quebec) and eight American states—Minnesota, Wisconsin, Illinois, Indiana, Michigan, Ohio, Pennsylvania and New York. A report in 2003 counted 148 federal and 51 state programmes to restore the lakes. The region's many swing states ensure periodic attention. In 2004 George Bush ordered a broad restoration plan to be drawn up. Implementing it would cost more than $20 billion. Little money, however, has been provided. It is still unclear who is in charge.

This may begin to change. On June 13th the secretary of state, Hillary Clinton, announced that a treaty governing the waters between America and Canada would be updated. Mr Obama's $475m would be the largest single investment of any president yet. Mr Davis, a respected advocate, may bring order to disjointed programmes.

Just as promising, restoration is increasingly seen as an economic boon, not a drain. The Brookings Institution, a think-tank, found that spending $26 billion to clean the lakes would bring benefits of at least $80 billion. As manufacturing dwindles, the lakes may attract new firms and workers. Chicago's twinkling lakefront has been an important draw, a taste of the Mediterranean in the Midwest. Indiana's shore is still lined with steel plants and refineries. But Portage's beach, which opened last year, is the first step in an effort to reclaim the lakefront. The new plans are a nudge in the right direction.

Gays and the census

Counting them in

Jun 25th 2009 | NEW YORK
From The Economist print edition

But they had hoped for more from the new president

AP

Not happy

"WE'RE getting impatient, and we're getting concerned," says Pamela Brown of Marriage Equality USA, a gay-rights organisation. "Rhetoric isn't going to work." Barack Obama was a vocal proponent of gay rights during his campaign. But they did not find their way onto the president's agenda until this month, when nerves had already started to fray; and now he is accused of not having done enough.

On June 19th officials announced that same-sex married partners would be counted in the ten-yearly census for the first time. The 2010 census will provide the federal government's first official recognition of gay marriage, which is legal in six states. Past censuses have not reported data on gays who consider themselves married. In the 2000 census, gay couples who ticked the box "married" were reclassified as unmarried partners. In the 1990 census, the Census Bureau changed the sex of one of the partners so they were counted as heterosexual—on the grounds the form-filler had doubtless made a mistake.

Gay activists and demographers cheered the administration's announcement. There are some 780,000 same-sex couples in the United States, around 10% of whom are officially married or in civil partnerships, estimates Gary Gates, a demographer in the law school of the University of California, Los Angeles. But no actual federal statistics have been available on the number of gay married couples, or their race or family size.

William Frey, a demographer at the Brookings Institution, says the census will "open people's eyes" to the number of gays living in the United States and make some policy issues, such as marriage, harder for politicians to dodge. On June 17th, Mr Obama announced that he will extend some (although not full) benefits to the same-sex partners of federal employees. But some gays worry that Mr Obama has not touched bigger issues, like his campaign pledge to repeal the "don't ask, don't tell" policy that bars openly gay people from serving in the armed forces, and the Defence of Marriage Act, which defines, for federal purposes, marriage as between a man and a woman. Gays, while they are happy to be counted, are beginning to worry that they cannot count on their president.

Statewatch: Washington

Not by aircraft alone

Jun 25th 2009 | SEATTLE
From The Economist print edition

The recession hit late but hard in Washington state

AP

WASHINGTONIANS like to point out that they are home to the largest building, by volume, in the world, a Boeing hangar in the Puget Sound north of Seattle. But Boeing and Washington, where the aerospace company was founded 93 years ago, have long had a love-hate relationship, and if the firm, still the state's largest private employer, appeared last year to be saving Washington from the recession sweeping the rest of the country, those hopes died in September.

They did so with one of the machinists' strikes for which Washington, where the union-friendly closed shop is legal, has an unfortunate reputation. Boeing's assembly lines ground to a halt. Within weeks the wider economic crisis arrived in the state with full force. A local bank, Washington Mutual, known throughout the state as "WaMu", became America's biggest banking failure. Starbucks and the other local notables looked glum. Even Microsoft began laying off workers. By May the state's unemployment rate was running at the national average of 9.4%.

In a state that has no income tax, the resulting shock to consumers had immediate ramifications, as sales-tax receipts plummeted. Tax "leakage" to neighbouring states such as Idaho or Oregon, which has an income tax but no sales tax, may be increasing as people who live on one side of the border shop on the other. Since Washington's tax set-up is regressive—"the most unfair tax system in the country", according to Lisa Brown, the Democratic leader of the state Senate—it is the poor who are clobbered hardest. And Washington has had to grapple with a budget deficit now larger in proportion to its population than even California's.

Relatively speaking, though, Washington is still in good shape, says Michael Parks, the editor of *Marple's*, a north-western economic newsletter. Neighbouring Oregon, more dependent on technology hardware as opposed to software and on the timber business, which crashed along with house construction, is much worse off, its jobless rate second only to Michigan's. And the entire Pacific north-west is suffering far less than the "sand states" (California, Nevada and Arizona) from foreclosures and bad mortgages.

Washington's economy tends to move according to its own cycles. One is the aerospace cycle, and Boeing, whatever troubles its airline customers are having, still has a backlog of orders. Another is the global economy. Washington is the country's most trade-dependent state, with one in four of its residents directly or indirectly reliant on trade, according to Dick Conway, an economist in Seattle. As America exported its recession to the world, Washington has imported it back in.

The good news is that all this trade is now far more diverse than it was in the 1980s, when the entire state was in effect a "company town". If Boeing, which in a fit of sulkiness moved its headquarters to Chicago earlier in the decade, were now to relocate even its assembly out of state—possibly to the South, where its European rival Airbus has already set up shop—Washington's various distinct economies could absorb the shock.

In particular, the Puget Sound economy around Seattle is home to an impressive cluster of world-beating companies. Besides Microsoft and Starbucks, there is the online retailer Amazon and offline retailers such as Nordstrom and Costco. With its views of Mount Rainier, its nearby nature and the water playground of the Sound itself, not to mention the lack of income taxes, the area is likely to be a perennial favourite of bosses and entrepreneurs.

Spokane, in the state's east, is the de facto service centre for inland Washington, Idaho and Montana, an area that once considered becoming its own state, "Columbia". The rural parts have the most fertile farmland in America outside of California's Central Valley, thanks to their volcanic soils. Washington is the country's largest producer of apples, raspberries, plums and hops. It makes good wines and a wheat vodka that locals swear is the world's best. As Mr Parks points out, much of Washington's economic history is about making comebacks, starting with the shift from making bombers during the second world war to making commercial aeroplanes thereafter. One or two more shifts may already be under way.

Lexington

The senator-in-chief

Jun 25th 2009
From The Economist print edition

Barack Obama is too deferential to his former colleagues on Capitol Hill

Illustration by KAL

THE easiest way for a president to make his life miserable is to antagonise his fellow politicians on Capitol Hill. Bill Clinton tried to steamroll Congress into passing a baked-in-the-White House version of health-care reform. Congress took one look at his 1,342-page draft bill and decided it had better things to do. Jimmy Carter treated Congress as an embodiment of everything that was wrong with American politics. Congress responded in kind.

Barack Obama has clearly learnt a lesson from his two Democratic predecessors. One of the earliest signs of the impending troubles between Mr Carter and Congress came at a breakfast that the newly elected president threw for congressional leaders. Tip O'Neill, the speaker, was appalled to find that the only victuals available were coffee, juice and a roll. "Hell, Nixon treated us better than this!" he roared—and demanded bacon, sausage, eggs and toast. Mr Obama has made a point of entertaining generously. Matt Bai, of the *New York Times*, says that he has created "the most Congress-centric administration in modern history". Thomas Mann, of the Brookings Institution, calculates that by late April, Mr Obama had already had personal meetings with more members of Congress than George Bush managed in his eight years in Washington.

As the first president to be elected from the Hill since 1960, Mr Obama has surrounded himself with congressional colleagues. Joe Biden, his vice-president, spent 36 years in the Senate. Rahm Emanuel, his chief of staff, was chairman of the House Democratic caucus. Pete Rouse, one of his most senior advisers, is a former chief of staff to Tom Daschle, and has been a fixture on the Hill since the early 1970s. Peter Orszag, his budget chief, is a former head of the Congressional Budget Office. Numerous other aides have deep roots on the Hill.

So far Mr Obama has been happy to leave much of the legislative heavy lifting to Congress. But he makes sure his aides work closely with their congressional colleagues. He occasionally resorts to the bully-pulpit to chivvy legislation along: this week he hammered away at the importance of health-care reform at a press conference on June 23rd and held a televised town-hall meeting in the White House on the health-care crisis next day. But he argues that his job is to lay down a broad agenda and let Congress fill in many of the details.

This has got things done fast, including a $787 billion stimulus bill, a $3.6 trillion budget and an expanded health-care programme for children. A cap-and-trade bill is well on the way to passing in the House. It has also helped to shield Mr Obama from criticisms from his own left flank. But the administration is also learning that deferring too much to Congress can produce as many problems as deferring too little.

The problem with Congress is that it is a many-headed monster, ill-suited to making hard choices or producing neat solutions. Individual members of Congress are more concerned with their own districts than with the future of the republic. The chairmen of committees are obsessed with defending their turf. The House is dominated by veteran liberals, who are well to the left of the electorate, and the Senate is full of prima donnas. Around 40 members of Congress have spouses who work in the health-care industry, as did Michelle Obama.

Mr Obama's Congress-centric approach has also taken a serious toll on the quality of his policies. The cap-and-trade bill does not do nearly enough to limit carbon emissions from politically powerful industries. The recent reforms of the financial regulatory system fail to tackle one of its most conspicuous weaknesses—its complexity—because doing so would mean stripping congressional committees of their oversight powers.

Health scare

But the toughest test of Mr Obama's approach will be health-care reform, the centrepiece of his domestic programme. He had hoped to subcontract the issue to two Senate veterans who know both Congress and health care better than anybody else in the country: Mr Daschle, whom he tapped to be both health secretary and health-reform tsar, and Senator Edward Kennedy. But Mr Daschle ran into tax problems and was unable to take up the jobs, and Mr Kennedy is seriously ill. Now two competing health-care bills, both unacceptably expensive in their current forms, are winding their way through the Senate and seem to be on a collision course, while in the House there is a third bill that must be melded into a compromise Senate version. Mr Obama's goal of getting this done by the summer recess seems to be receding fast.

There is no ideal way to reconcile the competing claims of the executive and legislative branches of government; America's system of checks and balances is a puzzle without a right answer. The Obama administration can argue that its governing style has produced plenty of successes, not least a timely response to the most serious financial crisis since the 1930s. It can also point out that Mr Bush, who emphasised "energy in the executive", succeeded in passing lots of bad and expensive legislation, but failed to reform either Social Security or immigration policy.

But a little more assertiveness on Mr Obama's part would be no bad thing. It is hard to see how he can bring spending under control without roughing up Congress a bit. It is also hard to see how he can fulfil his promise to be a post-partisan president while he continues to give so much power to Democratic barons. Back in 1962, when he tried to rank America's presidents according to their merits, Arthur Schlesinger concluded that "mediocre presidents believe in negative government, in self-subordination to the legislative power." Mr Obama does not give the slightest impression of being a man who wants to go down in history as a mediocre president.

Economist.com/blogs/lexington

Coca and cocaine in the Andes

Mixed signals among the coca bushes

Jun 25th 2009 | BOGOTÁ, LA PAZ AND LIMA
From The Economist print edition

An apparent fall in cocaine production conceals the remarkable resilience of an illegal industry

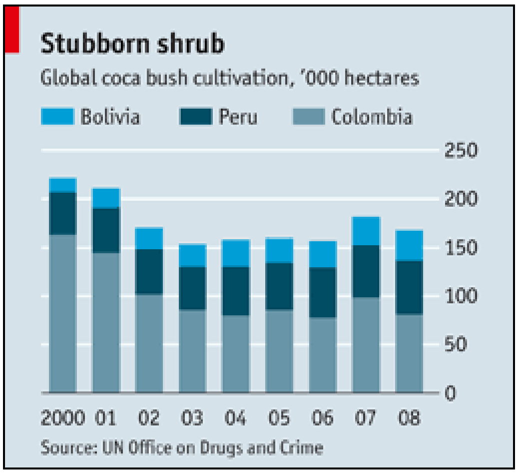
A YEAR ago when the United Nations' annual survey showed a rise of 27% in the area planted with coca in Colombia in 2007, the government expressed "serious doubts" about the reliability of the estimate. On June 19th Colombian officials were so proud of the UN's finding of an 18% decrease last year that they rushed to announce it five days ahead of its scheduled release. Although cultivation of coca, the hardy shrub from which cocaine is refined, is reported to have increased in Peru and Bolivia (see chart), the UN claims that lower yields mean that 28% less cocaine was produced in Colombia. Taken together with an estimated fall of 19% in opium-poppy cultivation in Afghanistan, the UN's Office on Drugs and Crime (UNODC) calls the results "encouraging".

That is surely welcome for UNODC, especially because it comes as the agency's worldwide policy of drug prohibition, reaffirmed at a ministerial meeting in April, is being increasingly questioned in Latin America and beyond (see article). In fact, there may be less to the headline figures than meets the eye.

Two things seem to lie behind the fall in coca cultivation in Colombia. Aldo Lale-Demoz, the UNODC's man in Bogotá, says the main factor is a greater stress on manual eradication, where workers physically yank up the coca, bush by bush, often in small plots on steep Andean mountainsides. This is more effective than aerial spraying, in which planes dump weedkiller, killing a harvest (and nearby food crops) but not the shrubs. On taking office in 2002, Álvaro Uribe, Colombia's president, launched a massive programme of aerial spraying. Last year the government still sprayed 133,000 hectares (330,000 acres), though this was 13% less than in 2007. But it also manually eradicated 95,634 hectares, a rise of 43% compared with 2007.

A second factor, according to Ricardo Vargas, a drug-policy analyst, was the success of the security forces in reducing the FARC

guerrillas, disrupting their control of territory and their drug-production operation. This allowed the government to get eradication teams into the eastern province of Meta, where coca has long been widely grown, and to pull up half of the crop there.



Progress in Colombia is partly offset by developments further south. Peru's steady upward trend in coca cultivation continued, even though President Alan García's government manually eradicated 10,143 hectares last year. Output is rising fast in the Apurímac and Ene valleys, which not coincidentally are home to part of the remnants of the Maoist Shining Path guerrillas, who terrorised Peru in the 1980s and 1990s. Nearly 40 soldiers and police have been killed in the area since the government began an attempt to regain control last September. In the Huallaga valley further north, where the Shining Path is also present, the government has pressed ahead with forced eradication, but in the Apurímac and Ene it feared social unrest.

Cultivation has also risen in Bolivia, but not by much, despite the government's expulsion last year of America's Drug Enforcement Administration (DEA), whose agents it accused of meddling. Bolivia's president, Evo Morales, who doubles as the leader of the coca-growers' union, insists that he is opposed to cocaine, though not to coca (which is traditionally chewed by Andean Indians). Both drug seizures and the number of anti-drug operations by Bolivia's police have increased under Mr Morales, though from a low base. The police recently destroyed a huge Colombian-run cocaine laboratory. But the lab's existence seemed to confirm the worries of American officials that despite these efforts the government's friendliness to coca growers helps the drug traffickers.

The apparent fall in coca production comes amid signs that Mexico's crackdown against drug gangs has had an effect in the United States, the biggest retail market for cocaine. America's DEA reports that the average purity of the cocaine it seized on the streets fell from 67% in January 2007 to 44% in December 2008, while the average retail price doubled to $200 per gram of pure cocaine. However, there have been several upward spikes in the retail price over the past two decades that have bucked but not broken a long-term falling trend. The retail price has recently also risen in Europe.

But it would be wildly premature to conclude from this year's figures that the Andean coca industry is in retreat. To sustain the fall in coca cultivation in Colombia requires the rule of law to take deeper root in rural areas, for eradication to be backed by offers of "alternative livelihoods" for coca farmers, as well as for demand for cocaine to continue to fall, says Sandeep Chawla, the UNODC's director of policy and public affairs.

In Meta Colombia's government has been quick to offer alternatives to coca. In Peru's Huallaga valley over the past two decades the authorities have helped thousands of farmers to replace 81,000 hectares of coca with alternatives such as coffee, cacao, rubber and oil palm. This success, says Rómulo Pizarro, who heads Peru's anti-drug agency, is because the farmers, different levels of government and foreign donors all worked together. Last month ministers unveiled a $115m plan to improve social provision and roads in the Apurímac and Ene valleys. But local mayors say that is not enough to counter the lure of drug trafficking. Experience shows that alternative development works only where it goes hand in hand with security and transport links to markets.

The problem is that the drug industry reacts to eradication programmes by pushing into new territory. The UN says that 59% of the coca it detected in Colombia last year was in areas where the crop had never before been planted. Now coca is springing up in several far-flung parts of Peru, including some national parks in the jungle. Adam Isacson, who follows Colombia for the Center for International Policy, a think-tank in Washington, DC, says that coca cultivation could well rise this year, because the FARC has regained control of some areas and because farmers lost their life savings in the collapse of financial pyramid schemes late last year. This week seven police died in a FARC ambush.

Estimates of drug production are far from foolproof. The UN derives its data from satellite photography, taken in December each year, backed up by field visits to sample sites. This methodology is more thorough than that used by America's Central Intelligence Agency, which provides the United States' government's estimates of drug production. But coca growers adapt to eradication by switching to smaller plots that are harder to spot.

Another doubt concerns how much cocaine is manufactured each year. Just as wine vintages vary, so the

weather can affect the number of harvests a coca plant yields and the alkaloid content of the leaves. And the effectiveness (or lack of it) of law enforcement can determine how much is processed. By interviewing some coca farmers, the UN concluded that yields fell in Colombia this year. This leads it to estimate that cocaine production last year totalled just 845 tonnes (down from 994 tonnes last year).

Mr Chawla concedes that this is an “uncertain measure”. There is much anecdotal evidence pointing to rising productivity. Eradication teams in Colombia talk of finding high-density coca fields in new areas, and more use of fertiliser by growers. Yields in the Apurímac and Ene valleys, where cultivation is expanding, are among the highest in the Andes.

All this counsels against reading too much into this year’s figures. Broadly speaking, the picture is one of a remarkable resilience in coca and cocaine production, despite enormous and hugely expensive efforts by governments to stamp it out. That resilience comes at a high cost in lives and environmental destruction.

Drug policy in the Americas

At last, a debate

Jun 25th 2009
From The Economist print edition

And an intemperate defence of prohibition

Agencia Estado

Cardoso calls for new thinking

EVER since George Bush senior launched “the war on drugs” in earnest two decades ago, Latin American governments have been more or less willing belligerents. That was partly because of the carrot and stick of American aid and bullying, but mainly because they suffer the brunt of the violence and corruption inflicted by trafficking mafias. Yet now there are signs of a rethink.

The clearest came in February when the Latin American Commission on Drugs and Democracy, a group headed by three former presidents—Fernando Henrique Cardoso of Brazil, César Gaviria of Colombia and Ernesto Zedillo of Mexico—published a report arguing that the violent crime and corruption generated by drug prohibition is undermining democracy and that the drug war has “failed”. They called for a public debate on alternatives, including treating drug use as an issue of public health rather than criminal law, and decriminalising marijuana.

This approach is gaining adherents. At least one minister in Brazil’s government agreed with the report. Even as it battles the drug gangs, Mexico has decided that people caught with small amounts of drugs should be treated rather than prosecuted. Argentina and Ecuador are considering more radical decriminalisation. Mr Cardoso, who has retired from political office, has since gone further than the commission and called for the decriminalisation of cocaine. He says that many active politicians privately agree with him. And in the United States, the Obama administration has signalled a shift away from drug “war” and mass incarceration and towards policies that treat drugs as a health issue.

This fracture in the taboo on questioning drug prohibition seems to have rattled Antonio Maria Costa, the boss of the United Nations Office on Drugs and Crime. In his preface to the annual World Drug Report, released this week, he concedes that drug users need “medical help not criminal retribution”.

But he also implies that proponents of drug legalisation—who include *The Economist*—are really seeking fresh sources of tax revenue to rescue failed banks. (No, Mr Costa, to pay for drug treatment and education.) Grotesquely, he equates legalising drugs and human trafficking. (Drugs primarily harm the user whereas trafficking harms others.) He claims legalisation would “unleash a drug epidemic in the developing world”. (That is what prohibition is achieving, because the criminal gangs it generates in developing countries have started supplying their local markets.) He smears his critics as “pro-drug” (as absurd as suggesting he is “pro-crime”). This kind of hysteria smacks of an organisation that is not just losing an unwinnable war but losing the argument.

Venezuela's media

Chávez's bugbear

Jun 25th 2009 | CARACAS
From The Economist print edition

The harassment of Globovisión

TO CRITICS who call him an autocrat, Venezuela's leftist president, Hugo Chávez, responds by pointing to a largely uncensored opposition media. Yet it is an argument that is wearing thin. Mr Chávez recently vowed to curb what he sees as the excesses of Globovisión, a 24-hour news channel that is his main bugbear. Closing it down may be the only way to do so.

Globovisión is the last remaining national channel that is critical of the government. It was one of four such channels that during Venezuela's political conflict of 2002-04, to varying degrees, egged on an opposition that was determined to oust Mr Chávez. Two have since capitulated, firing controversial talk-show hosts and adjusting their news coverage. In 2007 the government's broadcasting regulator refused to renew the licence of the fourth—Radio Caracas Televisión, which is now subscription-only.

Meanwhile, the government has built itself a huge media empire. Of the dozen free-to-air national television channels it controls six, as well as hundreds of radio stations and dozens of newspapers and magazines. These pump out pro-Chávez propaganda, interspersed with diatribes against the opposition and smears aimed at those who cross the president. In addition, the president has decreed his right to interrupt all radio and television broadcasts, without notice, for as long as he likes. These presidential *cadenas* (broadcasts) total almost 3,000 hours—the equivalent of an hour a day, six days a week, for the ten years Mr Chávez has been in office, according to Antonio Pasquali, a media specialist.

Even so, the government portrays itself as the victim of media terrorism. The president recently ordered mayors and state governors to provide him with a "map of the media war", showing which regional outlets are "in the hands of the oligarchy". Last month he instructed not just his ministers but also several nominally autonomous state bodies to move against Globovisión. Within days, the channel and its main owner faced a legal assault.

AFP

Hugo's idea of good television

The tax office imposed a fine of over $2.3m for non-payment of taxes on income the channel says it did not receive. After a public collection was launched to pay the fine, the authority doubled it. Guillermo Zuloaga, Globovisión's chairman, has been charged with "profiteering" in relation to his part-ownership of a Toyota dealer. Venezuela's most senior detective personally led a night-time raid on one of his properties. The channel's legal counsel, Perla Jaimes, has been indicted for "obstruction of justice" for insisting the terms of the search warrant be respected. Mr Zuloaga is even being investigated for environmental crimes because he has some old African hunting trophies. The biggest threat comes from the broadcasting regulator, Conatel, which has launched three separate investigations of the channel, each of which could result in a penalty of a 72-hour shutdown. A second penalty would result in its licence being revoked.

Globovisión has faults. Although its reporting is professional, its commentators are sometimes shrill and monotonous. Its owners abuse their power to choose which opposition voices are heard and which not. It is not much of an exaggeration to say, as government spokesmen do, that it behaves as if it were a political

party. But contrast it with the government channels, which are both turgid and inflammatory, and it is a journalistic paragon.

Some officials think that shutting down Globovisión would be a big mistake. It commands less than 10% of the audience (partly because it is free-to-air only in Caracas and Valencia). The damage to Mr Chávez's "revolution", these officials say in private, would outweigh the benefits. But the president claims his popularity would reach 80% (rather than its current 50% or so) were it not for "media lies". Globovisión must mend its ways, he insists. "Its time is running out".

Municipal corruption in Canada

Water and grime

Jun 25th 2009
From The Economist print edition

Montreal's mayor under pressure

BACK in the 1940s and 1950s Montreal was notorious in Canada for municipal graft. Recent allegations in Quebec's largest city remind some of those days. The police have five separate investigations under way into suspected fraud, kickbacks and favours involving tens of millions of dollars. Two of the probes touch former sidekicks of Gérald Tremblay, the mayor since 2002. Few suspect that Mr Tremblay, with a long previous career in Quebec's Liberal party, is crooked, and there is no evidence of that. But *La Presse*, the main federalist paper in Montreal and once a staunch supporter of the mayor, has twice called for him to resign. He shows no sign of doing so.

The scandals centre on construction firms thought to have underworld ties. The mayor's chief of staff was suspended last year over allegations that he organised the sale of municipal property for a fraction of its real value. One 38-hectare site, valued at C$31m ($27m), was sold for C$4.4m to a developer who not long before had been photographed by police with Nicolo Rizzuto, an octogenarian mobster and father of Canada's top mafioso. (The developer also has a record of evading taxes, issuing false bills and bribing officials.)

The second involves a C$356m contract to control water use by installing meters in commercial properties and by building underground valves. The contract went to a consortium led by Tony Accurso, an old friend of Frank Zampino, who headed the city council's executive committee. Before and after the contract was awarded, Mr Zampino and his wife holidayed on Mr Accurso's yacht. Mr Zampino then left politics and took a job with the other company in Mr Accurso's consortium for a salary of C$400,000. *La Presse* has marshalled evidence suggesting that the works could be done for a third of the price. Mr Zampino has since resigned from his new job. Both men deny any wrongdoing.

The mayor has suspended the contract pending an audit. He has also rounded on *La Presse*, accusing it of "a hidden agenda" to get rid of him. After the paper this month claimed that a contractor repairing the roof of city hall was shaken down for a C$40,000 bribe, Mr Tremblay said: "It's not up to *La Presse* to elect the mayor of Montreal, but the citizens." Polls suggest that when they do so in November they may shun Mr Tremblay for Louise Harel, a left-wing Quebec separatist.

India's Naxalites

A ragtag rebellion

Jun 25th 2009 | HARIHARPUR
From The Economist print edition

There are not enough brave politicians, honest officials and well-trained police to fight India's Maoist insurrection

AP

SQUATTING on a string bed in Hariharpur, a hamlet of West Bengal's West Midnapur district, Chhatradhar Mahato does not seem a hunted man. He is skinny, soft-spoken and, in a bored sort of way, lists the demands issued to the state's communist rulers by his group, the People's Committee Against Police Atrocities (PCAPA), which represents local *adivasis* or members of India's tribal minorities. Above all, Mr Mahato wants the local police, who in recent months have ceded a vast area covering some 2,000 villages to a joint force of PCAPA and Maoist guerrillas, to atone for their abuses by crawling to Hariharpur on their hands and knees. Their commander, says Mr Mahato, squatting before a poster of Mount Cook with an image of a Hindu priestess pasted onto its snowy summit, will have to perform penitential sit-ups while clutching his ears.

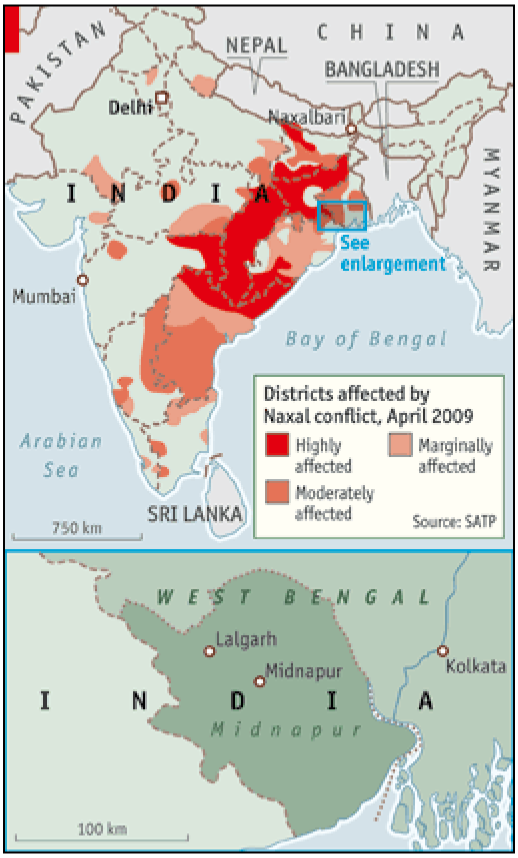
A short walk (or 15-minute crawl) away, in the village of Lalgarh, along a road blockaded by a few felled trees, hundreds of state police and central-government paramilitary troops are massing. They reached the village on June 20th, during an operation to regain control of the area. Though Mr Mahato denies it, the PCAPA seems little more than a Maoist proxy.

It has brutally quelled local opposition to the Maoists. Mr Mahato's younger brother also happens to be a notorious guerrilla, wanted for the attempted assassination of West Bengal's chief minister, Buddhadeb Bhattacharya, in Midnapur last November. The PCAPA was formed within days of that landmine attack, ostensibly to protest against the police's heavy-handed response to it. The senior Mahato and his fellow "committeemen" may face arrest for murdering around 20 supporters of West Bengal's ruling Communist Party of India (Marxist), or CPI(M), shot or beaten to death in the unrest. At least ten have been killed this month.

By the standards of India's Maoist insurrection, which affects roughly a third of the country's 604 districts and has claimed around 450 lives this year, that is a modest toll. Yet the events in Lalgarh have generated huge publicity in India. That is partly because West Bengal, where the Maoist insurrection was launched in 1967 in the village of Naxalbari (hence their nickname: Naxalites), has hitherto been resistant to it. This is in

turn a result of the strict village-level control exerted by the CPI(M), whose leftist coalition has ruled the state for over three decades. But the CPI(M) is struggling to maintain its grip, leading to its disastrous showing in India's general election last month. Now some fear the Maoists' influence could quickly spread.

Poor, barren and largely neglected by the government, West Bengal's tribal areas are just the sort of place where Naxalites thrive. The land around Lalgarh can be farmed for only three months of the year, leaving the locals heavily reliant on harvesting firewood, honey and *tendu* leaves, used for rolling *bidis*, crude cigarettes. Most are illiterate, and, owing to administrative corruption, incapacity and incompetence, see little benefit from welfare schemes earmarked for them. "There are a lot of lacunas," admits Manoj Verma, Midnapur's police chief. The Maoists have sought to fill them. Even as its blockade has brought government schemes to a halt, the PCAPA has tried to launch others, such as irrigation projects, paid for by money extorted from businessmen and officials—including the formerly bunkered-down police.



As this should suggest, the Maoists could not have overrun the area around Lalgarh if the state government had tried harder to stop them. West Bengal's policing is at best inadequate, with around 80 officers per 100,000 people, compared with over 250 in most developed countries. Yet the main reason for the government's failure is political. In the past two years, the Communists have been badly hurt by two protest movements against their efforts to acquire land for industrial development. In both cases, local resistance was fanned by their thuggish efforts to quell it and by their main political opponent, the Trinamul Congress party, as well as, to a lesser extent, by the Maoists. A third such debacle loomed after the attempted assassination of Mr Bhattacharya, who was returning at the time from the ground-breaking ceremony for a $7 billion steel plant in a tribal area near Lalgarh. The government therefore ordered Midnapur's authorities to go easy on the PCAPA/Maoists until after the election.

This has made shifting them from Midnapur harder than it should be. Mr Verma, the police chief, estimates that 300 Naxalites have entered the district and trained a similar number of locals in fighting skills. In three clashes, on June 19th and 20th, the advancing police and paramilitaries faced landmine attacks and ambushes by up to 150 guerrillas. But no policeman has been killed. As elsewhere, the Naxalites seem no match for a well-armed force.

Ridding Midnapur of them, however, will be hard. For a start, Mr Verma says the local police will be quadrupled. Plenty of economic development is also promised. But such plans often founder in India. Moreover, despite the renewal of a ban on the Naxalites by India's central government on June 22nd, many Communist politicians are loth to condemn their fellows on the left. With a state election due by 2011, and vociferous Bengali intellectuals flocking to defend the PCAPA, West Bengal's rulers could be tempted into another dangerous appeasement.

Indian-held Kashmir

Grim up north

Jun 25th 2009 | SHOPIAN
From The Economist print edition

A revolting crime has renewed protests against Indian rule

OUTSIDE Shakeel Ahmed Ahangar's house in Shopian, an apple-growing hub in the Kashmir valley, mourners gather. Spying a foreign journalist, they yell "*Azadi*!" ("Freedom!"). The battle-cry of Kashmiri separatists makes an incongruous lament for Mr Ahmed's pregnant wife and teenage sister, who were raped and murdered on May 29th. Yet it is the inevitable one. Six decades after India secured the richest portion of Kashmir, its Muslim inhabitants miss no chance to tell it to leave.

Month-long protests over the crimes in Shopian stress the truth of this. The local police have been widely blamed for the crimes—and certainly they tried to cover them up. The women went missing while walking home from the family orchard. Their battered corpses turned up the next day, semi-clothed, on a riverbank that Mr Ahmed and his relatives had combed shortly before. Nonetheless, the police said the women had drowned in the knee-deep river. They fired tear-gas at a crowd that disputed this. After Omar Abdullah, chief minister of the Indian state of Jammu & Kashmir, initially endorsed this lie, mass outrage was assured. The protesters are as liable to cry "*Azadi*!" as "Hang the culprits!"—though the police accused of these crimes, unlike the 600,000-odd Indian army and paramilitary troops in Kashmir, are almost all Kashmiris.

Mr Abdullah swiftly recanted and set up a commission of inquiry into the killings. Its interim report on June 21st confirmed that the women had been raped and murdered, and found that four senior police officers and a laboratory worker had tampered with the evidence. They have been suspended, and the commission's final report is due within days. But protests will continue. On June 20th, the main opposition People's Democratic Party launched a fresh round against the army's draconian powers in Kashmir.

Reuters

Some in Delhi find this disorientating. The insurgency against Indian rule in Kashmir had recently gone quiet. Last year it still claimed 541 lives. But this was the lowest toll since early in the two-decade-long insurgency. Reduced Pakistani support for the militants is one reason for this, but war-weariness among Kashmiris is another. They may never love Indian rule, but some Indian officials think they are learning to live with it. As further evidence, officials cite the recent general and state elections in Kashmir. Both were unexpectedly peaceful and well-supported.

It is hard to know how significant that is. Today's anti-India protests—and even bigger ones a year ago—suggest that many, or most, Kashmiris still loathe Indian rule. Yet waning violence at least gives the Congress-led government of Manmohan Singh a chance to woo them. In its previous term, which ended with its re-election last month, its efforts were dismal. A dialogue with separatist leaders that it inherited from its predecessor fizzled. So, for reasons that had more to do with political chaos next door, did the peace process with Pakistan, launched in 2003, that had inspired it. A separate, unloved multiparty process, which the separatists boycotted, produced some sensible ideas for pleasing Kashmiris. But they were largely ignored.

For all that, Congress's return to power as a more dominant coalition leader has raised a bit of hope that it will do better. America is gently urging this—the new administration is more willing to push for peace in Kashmir than was its predecessor. So far, the evidence is minimally encouraging. On a visit to Srinagar on June 11th the home minister, Palaniappan Chidambaram, said he wanted Kashmir's state police to take more responsibility from paramilitary troops. On June 17th Mr Singh suggested he was willing to reopen talks with the separatists. Under house

arrest in Srinagar until June 23rd, the chief separatist involved in the earlier round, Umar Farooq, says he would welcome this. But he would surely prefer a more effusive invitation.

Taking aim at Dehli

Taiwan's president and China

Sorry, the offer's closed

Jun 25th 2009 | TAIPEI
From The Economist print edition

A truce in the chequebook war

SINCE he took office in May last year, Ma Ying-jeou, Taiwan's president, has presented himself as a peacemaker, seeking to ease tensions with China. This conciliatory approach has led to the first regular cross-strait flights, the opening of Taiwan to Chinese tourists and investors, and the attendance by a delegation from Taiwan as observers at the United Nations' World Health Assembly in May, for the first time since China took Taiwan's UN seat in 1971. Now, Mr Ma told *The Economist* this week, he believes China has even adopted the surprising policy of refusing requests from countries that recognise Taiwan to switch their diplomatic ties to China instead.

This would mark a big change. For decades China and Taiwan have tussled to win over countries, largely through financial inducements. It has long been a losing battle for Taiwan, which is now recognised by only 23 countries, mostly small, poor ones. China has 171 diplomatic partners, and does not allow them to have official relations with Taiwan, which has suffered a net loss of six supporters this decade.

Last year, Mr Ma declared a "diplomatic truce", meaning an end to the chequebook contest for recognition. In his inaugural speech he then stressed that better relations with China depended on its easing Taiwan's international isolation. China has not responded publicly and officially it still opposes any country recognising the Republic of China, as Taiwan calls itself. But China's stance has been put to the test in El Salvador. The newly elected president, Mauricio Funes, reportedly expressed interest before taking office on June 1st in switching recognition to China. Taiwan's press has also reported that Panama's president-elect, Ricardo Martinelli, has similar inclinations.

"We do see a measure of goodwill" from China, said Mr Ma. Presidential candidates had said they wanted to establish formal ties with China but "the mainland obviously declined their request for the sake of Taiwan." Mr Ma said that when he attended Mr Funes's inauguration in El Salvador, "everybody said that once he was inaugurated he would establish ties with the mainland". But he says the first thing Mr Funes told him was that he wanted to maintain relations with Taiwan. A senior Taiwanese official responsible for mainland affairs, James Chu, says he believes that overtures by two of Taiwan's allies to China have been resisted by Chinese officials for the sake of relations with Taiwan.

Mr Ma said "a real test" will be how China deals with the Vatican, Taiwan's only European diplomatic partner, and one whose global influence far exceeds the others'. China has long been keen to win it over, as long as the Vatican cedes some control over the appointment of Chinese bishops. But negotiations between the Vatican and China show little sign of an imminent breakthrough.

Mr Ma is due to embark on another diplomatic tour on June 29th to attend the inauguration of Mr Martinelli in Panama and visit two other allies, Honduras and Nicaragua. America, delighted at the calming of cross-strait tensions under Mr Ma, has allowed him to engage in activities outside his hotel during a stopover in Hawaii on the way back, reportedly including a meeting with the state's governor, Linda Lingle. China, however, has reverted to type. "We strongly oppose any countries having official contacts with Taiwan", said a foreign-ministry spokesman. The goodwill Mr Ma detects has its limits.

China's internet censors

Dammed if you do

Jun 25th 2009 | BEIJING
From The Economist print edition

Protecting China's innocents from smut, violence and the Dalai Lama

Illustration by Claudio Munoz

THE internet is full of stuff of which China's government disapproves. Yet there are 300m Chinese internet-users. Keeping the two apart has embroiled the Chinese authorities in a long cat-and-mouse struggle. Service-providers and internet cafés are closely supervised, and a wide array of filtering mechanisms already overlays the national internet architecture. A fresh initiative goes one step further. From July 1st every personal computer sold in China will have to come with new filtering software called Green Dam Youth Escort.

It has yet to be decided whether Green Dam must be pre-loaded, or left on a disk for users to install. But it has sparked an uproar. Chinese internet users have vented online their spleen at being nannied. Hackers are reported to have mounted repeated attacks on the website of Green Dam's developer. It has also received more than 1,000 harassing phone-calls, including death threats.

An American firm, Solid Oak Software, claims Green Dam includes stolen copyrighted code from one of its products, and has launched legal action. Computer makers are understandably reluctant to abet a massive censorship scheme, or to anger their customers with unwelcome software. Moreover, independent experts at the University of Michigan found Green Dam to be riddled with outdated code and security flaws that would leave computers at risk.

America's Commerce Department this week lodged a formal complaint with the Chinese government, asking it to rescind the new rule. The government stresses Green Dam's role in protecting young people from "unhealthy" and "poisonous" pornographic and violent content. But the Michigan experts found that it is also scans text for "politically sensitive" phrases.

Whether to do with Tibet, Taiwan, or Falun Gong, a spiritual sect, there are plenty of these, leading to sites deemed "harmful" by China. In a year of harder economic times and sensitive political anniversaries, the authorities are especially edgy. The thin and cautious reporting in the press of events in Iran suggests they are also nervous about access to news of political protest elsewhere.

Despite the opposition, however, which includes a grassroots attempt to organise an internet boycott in China on July 1st, the government remains undaunted, promising that technical flaws will be fixed and that Green Dam will go forward. It has also opened a second front, lashing out at Google for including a feature in its Chinese service that automatically completes search-query terms—it complains that this can lead users to sites containing pornography.

Google has long struggled to reconcile its corporate credo ("Don't be evil") with the onerous demands of China's internet regulators. It has promised to renew its efforts to keep in line with Chinese standards. But the company also has fair cause to wonder why it has been singled out. Its main Chinese competitor, Baidu, is just as good at finding smut.

North Korea's Myanmar links

Cocking a snuke

Jun 25th 2009
From The Economist print edition

Carrots, sticks and now a bullhorn fail to deter North Korea

ONE is an ageing North Korean cargo tub with more than one previous owner and a record of weapons trafficking. The other, shadowing the *Kang Nam 1* as it chugs slowly round China's coast on its way, it is believed, to a port in Myanmar via the Malacca Strait, is an American guided-missile destroyer, bristling with up-to-date radars and weaponry. But it is to be hoped that the captain of the *USS McCampbell*, reportedly taking over the tracking from a sister ship, the *USS John McCain*, has at least one old-fashioned bit of naval kit on board: a bullhorn.

The American ships are doing UN-approved duty. Resolution 1874, passed unanimously by the Security Council on June 12th permits the searching of North Korean cargoes on vessels on the high seas suspected of carrying illegal arms shipments. But, in what seems a nose-thumbers' charter, it requires the flag-owner's consent, which in this case is highly unlikely to be forthcoming. If the Americans cannot direct the *Kang Nam 1* with stern words to a nearby port for a search, they will have to hope a shortage of fuel forces it to dock.

The new restrictions on North Korea limit its weapons imports to small arms, and ban all arms exports, conventional or otherwise. They followed a provocative long-range missile test and last month a defiant claim of the country's second nuclear test. Puzzlingly, sensors failed to detect telltale gases that usually leak out within days of such a test, but that could be because North Korea is, troublingly, better at testing small nuclear warheads deep underground than observers had guessed.

The regime's ailing boss, Kim Jong Il, is preparing more fireworks: perhaps another nuclear test; almost certainly short- and medium-range missile firings. A new launch-pad being prepared in the west of the country would allow testing of intercontinental-range rockets to the south, instead of as now across the Pacific towards America, which has threatened to shoot down any that appear threatening.

Where will all this lead? China and Russia, angered at Mr Kim's nuclear antics, agreed to support sanctions on his illicit weapons trade, but want six-party negotiations that also include America, South Korea and Japan, as well as North Korea, to resume. North Korea says it will come to the table as a "proud nuclear power" with no intention of giving up its bombs. "Delusional" is how one senior American official describes Mr Kim's demand to be accepted as a nuclear power; South Korea and Japan concur.

Meanwhile the fear is that Mr Kim will resume (if he ever stopped) helping others with their nuclear work. Financial records show that Mr Kim co-operated with a network run by a disgraced former Pakistani scientist, Abdul Qadeer Khan, to help supply Libya with nuclear material for uranium-enrichment work before the country abandoned its weapons effort. A nuclear reactor Mr Kim was secretly building for Syria, one ideally sized for producing plutonium for bombs, was destroyed by Israel in 2007 just before its completion.

Some reports say the *Kang Nam 1* is carrying missile parts; others that it is shipping mostly small arms to the junta in Myanmar. Mr Kim has sometimes used Myanmar to trans-ship missile parts, and who knows what else, to Iran. But Myanmar itself is a headache now, too. Russia has agreed to build it a small nuclear-research reactor. The worry is this nuclear toing and froing could disguise another joint venture, with North Korea: the secret building of a reactor like both Syria's and the one Mr Kim has used to produce plutonium for his own weapons tests.

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Myanmar's beleaguered Karens

On the run

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From The Economist print edition

A brutal offensive brings Asia's longest civil war closer to its end

AFP

GOVERNMENT troops advance. Terrorised villagers flee. Rebels fight back. For six decades this has been the rhythm of warfare in eastern Myanmar, where ethnic-Karen insurgents fight the ruling junta. The latest offensive by Myanmar's army began in June and is unusual not in its ferocity but in its timing, in the wet season. The army, backed by a breakaway Karen militia, has managed to overrun several bases of the Karen National Liberation Army (KNLA). Since June 2nd some 4,000 civilians have fled the fighting and crossed the border into Thailand. There is talk of the rebels' Alamo moment.

The reasons for the junta's sudden haste are typically murky. It is preparing for parliamentary elections next year, the first since an annulled 1990 poll, and wants around 17 ethnic rebel groups that have signed ceasefires to take part. The Karen National Union (KNU), the movement's political wing, is a holdout. The generals, who want to consolidate power and neutralise armed threats, have proposed turning ethnic insurgents into border guards, under their command. They may reckon that the KNU can be similarly corralled. But a crushing military defeat would do just fine.

The offensive also appears timed to divert attention from the trial of Aung San Suu Kyi, the detained opposition leader. Thailand's foreign minister, Kasit Piromya, has been more strident than most in publicly dressing down the junta about this farce, which is due to resume on June 26th. Thai diplomats suspect that its prickly neighbour is stirring trouble on the border as a poke in the eye.

The KNLA serves as a useful buffer for Thailand's army. But Thai support for the Karens' lonely struggle may be waning. So far, villagers fleeing Myanmar's marauding troops have not been turned back. However, a wider collapse of the KNLA might well trigger a larger exodus into Thailand. Some 140,000 refugees, mostly Karens and Karennis, another ethnic group, are already confined to Thai camps built in the 1980s which have a depressing air of permanence. Some activists are critical of the faction-ridden KNU and its pandering to Christian aid groups. Certainly, bibles and workshops have not freed the Karen from Myanmar's yoke. It is hard to see what could.

Banyan

Burying Asia's savage past

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Balancing reconciliation with justice may be impossible. A tiny bit of either would be nice

Illustration by M. Morgenstern

FOR several weeks a neat former schoolteacher has sat in a Phnom Penh dock, detailing before the tribunal how meticulously he used to carry out the orders of his bosses. As a child, he said by way of clarification, he had always been "a well-disciplined boy, who respected the teachers and did good deeds". This is Kaing Guek Eav, alias Duch, former commandant of Tuol Sleng, a Khmer Rouge torture-centre and prison, which 14,000 men, women and children entered but only a dozen survived. Duch has admitted blame for the horrors at Tuol Sleng. According to the *New York Times*, he couldn't bear to hear the late Pol Pot claim that Tuol Sleng was a fabrication of his enemies. He thus seems certain to be the first person convicted for playing a part in Khmer Rouge atrocities from 1975-79 that killed up to 2m Cambodians.

This is not unqualified good news. Justice comes years too late. The United Nations and Cambodia haggled for a decade just over the details of the court, eventually set up in 2007. The costs have been gargantuan, though, according to its outgoing chief foreign prosecutor this week, it is still "underfunded and under-resourced". Political meddling is high, and corruption apparently abounds. Some of the senior Khmer Rouge leaders who gave Duch his orders await trial, but they are frail and may not live long. Besides, Cambodia's strongman leader, Hun Sen, is a former Khmer Rouge himself and may be unwilling to see too much dug up. Duch may be the first to be tried, but also the last.

Asia has plenty of killing grounds, and their story is similar. In Timor-Leste two truth-seeking commissions have looked respectively into the death of 200,000 people during Indonesia's scorched-earth occupation after 1975, and into an orgy of arson and killing by the Indonesian army and its vigilante henchmen after East Timorese voted for independence in 1999. By coming up with a record, and by even eliciting an admission of blame by Indonesia, the reports exceeded expectation. Yet many Timorese want a proper reckoning. Reconciliation can get in the way. The reports have gathered dust. Timor-Leste's present leaders argue that, with aid scarce, filling bellies trumps paying for tribunals.

Above all, they do not want to open old wounds. Timor-Leste's first president, Xanana Gusmão, who like Nelson Mandela was a former prisoner of the old regime, also followed Mr Mandela in calling for forgiveness. His successor, José Ramos-Horta, has since pardoned the very few men to have been imprisoned for the 1999 violence. A culture of amnesty prevails. There is little evidence that it has helped stability. On the contrary, Timor-Leste has seen gang warfare, a mutiny by part of the army and an assassination attempt on Mr Ramos-Horta.

Political leaders' wish to sweep the past under the rug is such an Asian habit that suspicions are aroused when a government seems too keen to try the opposite. Take Bangladesh. The Awami League under Sheikh Hasina wants to try 50 Bangladeshis for atrocities in the 1971 war of secession, in which perhaps 3m died. The suspects include nearly the entire current leadership of Jamaat-e-Islami, the biggest Islamic party and a former coalition partner of Sheikh Hasina's nemesis, Khaleda Zia. Jamaat-e-Islami's youth wing, in league with the West Pakistani army, specialised in killing intellectuals. Still, Sheikh Hasina's nakedly political motives would undermine a tribunal's credibility abroad.

In the end the international response makes, or more usually breaks, the search for justice, which almost always needs foreign support. Who, for instance, pays for reparations? In Cambodia it will not be the doddery former Khmer leaders. In Timor-Leste it was suggested that those who sold arms to the Indonesian army should stump up a share. And pigs may fly. As tribunal costs (and failures) mount, the United Nations and rich-world donors tend to slough off responsibility.

More than that, the process of justice and reconciliation is usually hostage to hard-nosed geopolitics. In private, diplomats from China, staunch ally of the Khmer Rouge and still Cambodia's chief patron today, put down the tribunal's aims. It is easy to forget how the United States also backed the Khmers Rouges as victims of Vietnamese expansionism. Support for the Indonesian army during the cold war meant that America overlooked atrocities in East Timor. That had changed by 1999. But after September 11th Indonesia, the scourge of East Timor, became a chief ally in the war against terror. A newly democratic Indonesia is hardly to blame for its army's past. Besides, many Indonesians were themselves victims of state-backed violence during the Suharto era.

Might is right

Similarly, hard-nosed geopolitics bodes ill for any accounting in Sri Lanka, now that the Sri Lankan army has defeated the Liberation Tigers of Tamil Eelam, with both sides accused of war crimes. For the process to start now is out of the question. Domestic critics of the army's conduct fear for their lives as "traitors". But the response of the UN Security Council was dismal during this year's military endgame, in which tens of thousands of civilians were trapped. Though the UN agrees that "timely and decisive" action should be taken when governments fail to protect their own people, lobbying for pressure on Sri Lanka by the West was mild, and cynical opposition to council action by China and Russia, two chief sellers of arms to Sri Lanka, was vigorous.

As for China itself, Banyan lived a decade ago in a Beijing compound whose backdoor guard, a soft-spoken bourgeois type, had not exchanged a word with the frontdoor guard, his tormentor during the Cultural Revolution, since the last ghastly struggle session in 1969. The era remains nearly off-limits for public debate, and the only reckoning was the show-trial of the Gang of Four in 1981. In that light, any attempt at a first draft of historical honesty, as in Cambodia or East Timor, looks far better than nothing.

Economist.com/blogs/banyan

The crisis in Iran

Is the dream already over?

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The authorities may succeed in quelling the street demonstrations. But the crisis is far from over, especially as the ruling clergy quarrel among themselves

Reuters

THE roller-coaster that liberal-minded Iranians boarded as they agitated en masse against a suspect presidential poll seemed to hit the buffers on June 20th, when a banned demonstration was met with lethal force. Millions of Iranians remain incensed by what they see as President Mahmoud Ahmadinejad's fraudulent victory over his main challenger, the reformist Mir Hosein Mousavi, in the election of June 12th. But far fewer now seem ready to take the risk of venting their anger on the streets. For all that, it may not take much to provoke another popular eruption. A fresh spark may yet be provided by the unusually public struggle for dominance over the Islamic Republic that has erupted within the ruling clerical establishment itself. The crisis may indeed be moving from the street to the back rooms of the mosque.

Aiming for a resolution of sorts, Ayatollah Ali Khamenei, Iran's supreme leader, and the man who has the last say on all matters of state, issued a dramatic ultimatum in a sermon on June 19th. Addressing a huge television audience, he dropped his customary pose of impartiality in electoral politics, siding with Mr Ahmadinejad and warning Mr Mousavi's supporters that further street protests would lead to "violence, blood and chaos."

To the surprise of many Iranians, who do not as a rule associate reformist leaders with political courage, Mr Mousavi refused to call off a demonstration that had been planned for the next day, nor did he retract his demand that the results be annulled and the election held again. But the result was a pitifully unequal struggle between demonstrators hurling stones and tens of thousands of Revolutionary Guards and voluntary militiamen, known as the *baseej*, armed with truncheons, water-cannon and automatic rifles.

According to state-controlled media, a score of people have been killed. Other reports put the figure much higher, and say that several hundred have been injured. The government said that 40 brave *baseej* had been hurt. Some residential areas in central Tehran resembled war zones. The protesters have exalted the image of a beautiful young woman, Neda Agha Soltan, who was photographed in a demonstration in Tehran as she lay dying after being shot by an unknown assailant.

An edgy calm has now descended on the city. Protests in Tehran and other towns, such as Isfahan,

Kerman, Shiraz and Tabriz, which witnessed huge displays of public dissent after the election result was announced, have since got smaller, letting the authorities tackle the people they regard as instigators of the troubles.

According to the Committee to Protect Journalists, a New York-based lobby, more than 40 journalists have been arrested since the elections and at least 450 political campaigners imprisoned, severely limiting the ability of Mr Mousavi and Mehdi Karroubi, the lesser of the two reformist presidential candidates, who is also demanding fresh elections, to plan their next move or even communicate with their supporters. Several senior colleagues of Muhammad Khatami, a reformist former president, have been arrested, along with at least a dozen journalists close to Mr Mousavi's campaign, according to a website that is tracking events.

Fearing a backlash, the authorities have so far refrained from arresting Mr Moussavi or Mr Karroubi. But they are laying the ground. Mr Mousavi has been savaged by the pro-government media and accused of helping a banned opposition group, the People's Mujahedin of Iran, which is particularly active in western Europe. On June 21st the head of parliament's judiciary committee said Mr Mousavi's public statements constituted "criminal acts". Tehran police claim to have found evidence of co-operation between "foreign elements" and agitators operating from a building that was used by the Mousavi campaign.

Neither Mr Mousavi nor Mr Karroubi had much faith in the willingness of the Guardian Council, a watchdog body itself watched over by Mr Khamenei, to investigate fairly their allegations that Mr Ahmadinejad owed his landslide victory to fraud. According to the Interior Ministry, the incumbent won 25m votes out of 39m cast, compared with 13m for Mr Mousavi and a risible 300,000 for Mr Karroubi, a former speaker of parliament. Scepticism is understandable: the council is in overall charge of running the elections, which means that it has been investigating itself.

Mr Mousavi says that the election was perverted by a multitude of procedural irregularities and by restrictions placed on his representatives' legal right to monitor ballot boxes. These allegations, which he put in writing, have had little effect. On June 21st a spokesman for the Guardian Council announced that in 50 towns the number of ballots cast had exceeded the number of eligible voters. But it was possible, he went on, that many people had voted outside their home towns.

The council may be preparing for a modest revision of the results, giving Mr Mousavi a few more votes, probably in a few days' time. But annulment, as Mr Khamenei made clear in his sermon, when he denied that the Islamic Republic "goes in for betrayal in the matter of the people's votes", seems out of the question.

Permitted little contact with their supporters, their precise whereabouts a matter of intense public speculation, Messrs Mousavi and Karroubi have managed at least to unnerve their opponents with their refusal to give up. Mr Mousavi has described defenders of Mr Ahmadinejad as "the proponents of a petrified, Taliban-style Islam" and has dismissed the idea, first expressed by the supreme leader, that the agitation was driven by foreign enemies. On June 24th Mr Karroubi defied a government ban by holding a wake for those who were killed in the violence four days earlier. But it was violently broken up.

The real new fight is less visible

So the battle for the streets may inevitably be heading for victory for Mr Ahmadinejad and the ruling clerical establishment behind him. But a titanic struggle behind the scenes, obscured by public events and often blurred by Tehran's whirring rumour mill, may be just as crucial to the country's future. This pits Mr Khamenei against a wily former president who until recently was often regarded as the Islamic Republic's second-most-powerful man, Akbar Hashemi Rafsanjani.

On the face of it, this struggle is also going the supreme leader's way, as you would expect, since between them Mr Khamenei and his president hold the main levers of civilian and military power. Mr Rafsanjani's long silence since the election suggests he has been disheartened by the verbal attacks on him and by the arrest of several family members, including his daughter, a former parliamentary deputy, who has since been released. Mr Ahmadinejad has made no secret that he longs to see Mr Rafsanjani and members of his family charged with corruption.

So complete is Mr Rafsanjani's eclipse, at any rate for the time being, that information on his movements and intentions now consists of hearsay. According to one account, he has been busy in the seminary town

of Qom, canvassing senior clerics to back a move to sack Mr Khamenei. Another suggests he may signal his surrender to the inevitable by attending Friday's prayers, whereas he was conspicuously absent when Mr Khamenei gave his sermon on June 19th.

In jail or at home, Iran's reformists must be rueing their mistakes. It was Mr Rafsanjani, after all, who helped manoeuvre his old friend Mr Khamenei into the vacant supreme leader's chair after the death of the revolution's father, Ayatollah Ruhollah Khomeini, 20 years ago. To that end, Mr Rafsanjani helped ensure the eclipse of Ayatollah Hosein Ali Montazeri, who had been Khomeini's heir apparent and who now, a fragile octogenarian, sends messages in support of Mr Mousavi's cause. Later, during the presidency of Mr Khatami (1997-2005), reform-minded Iranians turned on Mr Rafsanjani with such venom that he failed even to win a seat in parliament in the elections of 2000.

Have the liberals lost?

The price of those misjudgments and divisions will be high. Ever since the Islamic Republic was set up after the revolution of 1979, revolutionary purists have had to tolerate another faction, culturally more liberal and latterly more open to relations with the West. This lot is now being squelched.

At what cost to Iran's already tarnished image abroad? Thanks to their mobile telephones, the protesters have beamed the most gruesome images around the world. France's president, Nicolas Sarkozy, says the "repression and violence" is "unacceptable". Germany's chancellor, Angela Merkel, has expressed support for "the people in Iran who want to exercise their right to freedom of expression and freedom of assembly." Barack Obama, who had at first tried to stay aloof so as not to endanger his policy of detente with Iran, declared that he was "appalled and outraged…by the threats, beatings and imprisonments" being meted out. The protesters, he said, were "on the right side of history".

Reuters

Khamenei ponders his supremacy

For the many people in Tehran who had hoped that Mr Obama would help usher in a bright new chapter in relations between Iran and the West, this is depressing. Western criticism has bolstered those in Tehran whose instinct, at the first sign of trouble at home, is to seek foreign scapegoats. At the top of the list comes Iran's favourite bugbear, Britain.

Taking their cue from Mr Khamenei, who described Britain as "abhorrent" in his sermon, Iranian officials have accused Britain's government of sinister manipulation of events. Manuchehr Mottaki, Iran's foreign minister, described in outlandish detail how Britain had flown in planeloads of spies (he did not explain how they had cleared immigration); he then expelled a brace of British diplomats. Iran's foreign-ministry spokesman has depicted two foreign-based satellite television channels, BBC Persian and the Voice of America, which have been transmitting images and comment to viewers in Iran, as part of an Israeli conspiracy to break the country up.

America's choice

Mr Obama must now decide whether to let all this affect his efforts to engage Iran. His aim is to persuade the country to forgo its contentious nuclear plan—or at least to modify it and throw it open to scrutiny. Plainly, Israel's hawkish prime minister, Binyamin Netanyahu, senses a chance to help kibosh an American diplomatic initiative that discomfited him from the start.

Some Iranians who cheered Mr Obama's policy of engagement may have changed their minds. Shirin Ebadi, a Nobel peace-prize laureate who is Iran's best-known human-rights campaigner, has asked the European Union to freeze all political dialogue with Iran "until the violence stops and fresh elections are held." But Russia, which Mr Obama had hoped to draw into a coalition of countries tugging Iran towards respectability, is being awkwardly indulgent of Iran's behaviour, with a foreign ministry spokesman calling the crisis an "internal affair". More predictably China has endorsed the election.

Unless Mr Khamenei dramatically changes heart or protests resume on an irresistible scale, reform-minded

Iranians may again have to resign themselves to living without the limited democratic freedoms, including the right to elect a president from an albeit vetted field, that they had hoped to build on. A political elite shorn of its reformist element may well bolster the authoritarian and militarist ways that Iranians are already seeing in embryo: *baseej* militiamen on every street corner; a special court that is being set up to try arrested “hooligans”; and senior military people muttering darkly about foreign threats.

In the longer term, however, many Iranian liberals think Mr Obama’s optimism will be vindicated. The election campaign and the protests that followed have permitted Iranians to express themselves with a freedom they have not known since the revolution of 1979. They enjoyed the experience—and want more. Further, the sight of infighting among leaders who were apparently united under the binding influence of Ayatollah Khomeini, has undermined the Islamic Republic’s claim to legitimacy, and still more its claim to sanctity. “That idol has been smashed,” said a commentator in Tehran.

In any event, Mr Mousavi’s campaign is going on. If he is arrested, his supporters say they will call a general strike. At night, people around the country gather on their rooftops to shout “Allahu Akbar!” (“God is Great!”), a call dating back to the 1979 revolution that Mr Mousavi’s people have made their own. And many Iranians will fondly recall the post-election march on June 15th that as many as 2m people attended. It was impeccably well-behaved, good-humoured and entirely self-policed.

In the words of one Iranian who attended, “Before then I had lost my faith in being Iranian. We were becoming selfish, turning in on ourselves. But that march seemed to change everything. It can’t have been a dream—can it?”

Iran's debate over theocracy

Why the turbans are at odds

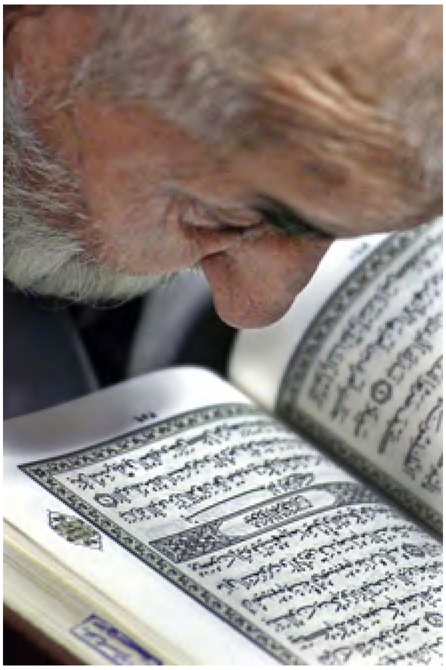
Jun 25th 2009
From The Economist print edition

A debate rages about the nature of clerical rule

THE Koran is the word of God, which every Muslim must follow, but its commands can be hard to interpret. So people should submit to the rule of a properly trained religious scholar. The idea is a simple one, and the father figure of Iran's revolution of 1979, Ayatollah Ruhollah Khomeini, made it the central principle of his Islamic state.

But the notion of *velayat-e faqih* (guardianship of the jurist) has proved to be controversial as a religious doctrine and tricky in practice. The turbulence now sweeping Iran has many causes, among them a simple urge for freedom. Yet the tensions, inconsistencies and hypocrisies generated by trying to impose *velayat-e faqih* lie at the heart of its troubles.

AP



Room for interpretation

Divisions among top Shia scholars are nothing new. In the main seminary towns of Najaf in Iraq and Qom in Iran, followers of competing ayatollahs have frequently clashed, sometimes with fists. One recurring split has pitted scholars who believe they should stay outside politics against those who believe they must engage in it. Ayatollah Khomeini pushed this argument to a new level. His revolutionary constitution created the post of supreme leader, placing an unelected senior scholar in overall command of the country.

Many of his fellow ayatollahs saw this as an "innovation", a bad word in Muslim jurisprudence, signifying an unsubstantiated departure from Islam's founding texts. Some feared that immersion in worldly affairs would taint clerics and end by repelling believers from the faith. Others argued that democracy was a better way to divine God's will, or that a committee of scholars, rather than a single man, would suit the leadership function better. Ali al-Sistani, a Najaf-based ayatollah who is probably the most widely revered scholar among the world's Shias today, has stated that in order to be legitimate such a ruler should win acceptance from a majority of believers.

Ayatollah Khomeini, who died in 1989, himself once declared the popular vote a measure of legitimacy and allowed for an elected parliament and president, as well as an Assembly of Experts theoretically charged with monitoring the supreme leader. But his successor, Ali Khamenei, despite lacking both the scholarly credentials and the revolutionary aura of Khomeini, has accumulated ever more power relative to Iran's elected institutions. Under his rule, questioning the doctrine of *velayat-e faqih* has become taboo. Scholars who query it openly or cast doubt on Mr Khamenei's fitness for the role have been dispatched to obscurity, exiled or imprisoned. The Guardian Council, the appointed 12-man body that vets candidates and elections, summarily disqualifies anyone seen as insufficiently devoted to the doctrine.

Yet opposition is still brewing. The doubters include not only leading scholars in the seminaries of Qom, but some of Ayatollah Khomeini's closest associates, including prominent members of his own family. Today's crisis, which has seen the supreme leader abandon the pretence of neutrality in favour of the hard-line faction behind Mr Ahmadinejad, has exposed doctrinal divisions as never before.

The cheated presidential candidates have appealed directly to the scholars of Qom without challenging *velayat-faqih* as a doctrine. But their direct defiance of Mr Khamenei is an unprecedented show of rebellion against how it is practised. The response from Qom has been mixed. One group of mid-ranking clerics has blasted the election as a fraud, and at least four of the 19 grand ayatollahs who bestride Iran's Shia hierarchy are said to agree. So far none but Mr Khamenei has openly endorsed the official outcome.

This does not mean the supreme leader is alone. Many Shia clergymen either depend on his largesse or hold loyalty to the state and its Islamic mission above matters of personal opinion. Besides, Mr Khamenei's tenure has seen power steadily drain away from the clergy and towards Iran's security services, whose commanders he appoints. But with rumours swirling of a lobbying campaign to rally clerical support for ousting Mr Khamenei, the supreme leader may suddenly find himself facing not only a backlash from the millions of ordinary citizens who now openly denounce him as a dictator, but also from his robed and turbaned comrades.

Security in Iraq

Is it getting worse again?

Jun 25th 2009 | BAGHDAD
From The Economist print edition

As American troops prepare to leave all the towns, Iraqis are getting nervous

BARACK OBAMA's administration has promised to withdraw all American troops from all of Iraq's towns by the end of this month. As the deadline looms, people are again asking whether Iraq's forces will be able to cope on their own. On cue, a fresh bout of violence has erupted. On June 20th, a huge lorry bomb exploded in Taza, a Turkmen town just south of the disputed city of Kirkuk, killing at least 70 people. Two days later at least seven bombs went off in and around Baghdad, including a roadside blast, a car bomb and a suicide attack, killing some 30 people altogether. And on June 24th another big bomb killed at least 70 people in Baghdad, perhaps the single deadliest attack in Iraq this year. The insurgents, knowing that the Americans are poised to pull out, are aiming to make Iraq as unstable as ever.

They have also staged some spectacular assassinations that have threatened to restart a cycle of sectarian reprisals. Earlier this month the head of the main Sunni bloc in parliament, Harith al-Obeidi, a noted campaigner for human rights, was gunned down by a teenager in a Baghdad mosque after he had led Friday prayers. In Mosul, the biggest city of the north, where the coach of Iraq's karate team was recently shot dead, bombings are still going on, though at a reduced rate.

Yet, despite this nerve-racking spasm, the recorded figures suggest that the violence is still in retreat. Fewer civilians were killed in May than in any month since 2003. Both Iraqi and American officials had predicted a surge in attacks as the deadline for withdrawal neared.

The prime minister, Nuri al-Maliki, told Iraqis not to be dismayed by violence here and there. The country's own forces, he insisted, could maintain security, as they already were. Besides, American tanks and armies were no use in what had become a counter-insurgency intelligence game, which the Iraqis were better equipped to play than were the Americans. "We're absolutely certain the withdrawal will not make our security worse," said Mr Maliki. In any event, he said, the withdrawal of American troops from the towns would be a "great victory" for Iraq.

In fact American troops have already withdrawn from nearly all the towns—and have rarely been seen in them of late. Many joint American-Iraqi security posts have been dismantled. There will be no more routine American patrols, rare though they have already become. The Americans will, however, remain in bases nearby, on call in case Iraqi forces hit trouble. And in some places, especially in Mosul, where efforts to suppress the insurgency have been intensifying, the definition of city limits is being elastically interpreted, to let the main American base stay where it is, on the city's edge.

But the Iraqis are slowly realising that Mr Obama really does intend to remove the bulk of his troops before 2011. So they may at last be starting to focus on passing long-delayed bits of important nation-building legislation, such as an oil-and-gas law, constitutional amendments, and even a law governing elections. Without a modicum of cohesion at the heart of government, how can Iraq's security forces stick together in the face of sectarian or ethnic tension? Iraqis know that establishing a more cohesive and broader-based government is at least as important as beefing up the Iraqi security forces.

A crucial general election is due in January—and everybody knows that the Americans want to witness a peaceful poll leading to a stable government before they can withdraw completely. So there is a fresh ferment of political horse-trading and alliance-testing. Mr Maliki is trying to buff up his image as the strongman who can provide law and order. He is exploring the possibility of new ties across sectarian divisions as well as sounding out possible partners for a grand Shia coalition similar to the one that won last time. Even the "Bands of the Righteous", an offshoot of the Shia militia movement led by a radical cleric, Muqtada al-Sadr, may want to take part in peaceful politics. As a gesture of goodwill, it released the bodies of two long-dead British hostages who had been kidnapped two years ago.

Yet, whether the Americans stay or leave, Iraq still suffers from its worst failing. There is still no party or leader that can reach across the country's divisions and appeal to Iraqis of every ethnic and sectarian hue.

Somalia and its jihadists

A government under the cosh

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From The Economist print edition

None of Somalia's neighbours is keen to ride to its rescue

THE fragile government of Somalia is in deep trouble and, according to one of its officials, "scared witless". Hence its panicky call on June 20th for troops from neighbouring Kenya and Ethiopia to come to its rescue or see the country fall into the hands of jihadist fighters linked to al-Qaeda. Hence, too, the reluctance of its diplomats to heed a call from their foreign ministry to return from abroad to Mogadishu, the capital, for "retraining". That was hardly surprising, since a teenage suicide-bomber had just blown up Somalia's ambassador-designate to South Africa, along with its interior minister.

Fighting in Mogadishu has again emptied the coastal city of many of its poorer inhabitants. A 4,300-strong force consisting mainly of Ugandans and Burundians under the African Union's aegis is unable to keep the peace. The government's own troops are ill-equipped and rarely paid.

By contrast, a commander of the jihadist group known as the Shabab (meaning "Youth") struck a cockier note, promising that foreign troops would be killed; Somali cats and dogs would eat them. "Somali young mujahideen," he said, "will fight any troops deployed here until our last holy fighter passes away." It is easy to see which side thinks it has the upper hand.

The Shabab's confidence and sense of direction has been boosted by an influx of foreign fighters. Aides of Somalia's embattled president, Sharif Ahmed, say there may be over 2,000 of them. Western intelligence sources think fewer. One of its bomb experts, Abu Mansour al-Amriki, appears to be a white American. Other al-Qaeda fighters have come from Pakistan and Afghanistan and may recently have helped assassinate Mogadishu's police chief as well as clan elders and local journalists. The group's slick internet propaganda echoes al-Qaeda. The Shabab says it has set up three units of suicide-bombers. At first they were mainly foreign but now they tend to be Somali boys educated in the movement's religious schools.

Kenya and Ethiopia are loth to step in. Neither can afford a big military offensive. Both have large Somali minorities. The Shabab says it downed a Kenyan military helicopter flying along the border last month, though Kenya denies it. In any event, the Shabab says it "will destroy the tall glass buildings in Nairobi" unless Kenya pulls its troops back from the border. Any terrorist attack would badly hurt Kenya's already shaky tourist industry and may well deter foreign investors. In any case, Kenya is unlikely to send its forces into Somalia unless it is attacked first.

Ethiopia withdrew most of its troops from Somalia earlier this year, after losing perhaps 800 of its men. A few Ethiopian soldiers are thought to remain discreetly inside Somalia, rallying armed opposition to the Shabab. But Ethiopia's government has no appetite for sending in troops all over again. Ethiopian officials dislike being portrayed as stooges for the previous American administration's war on terror and say their troops would return only under an international mandate and in smaller numbers. "We don't want to be the horse taking the chestnut out of the fire and then being whipped by everyone and his grandmother," says Meles Zenawi, Ethiopia's prime minister. Yet he cannot stomach a jihadist state across his border, backed by his enemy, Eritrea.

The last hope for Somalia's wobbly government may be the United States, which has once again secretly begun to supply it with arms. But that may be too late to save the day.

Germany's mediocre universities

On shaky foundations

Jun 25th 2009 | FRANKFURT
From The Economist print edition

The effort to improve German universities still has a long way to go

Illustration by Peter Schrank

THE IG FARBEN building in Frankfurt has a history. This is where Zyklon B gas, used at Auschwitz, was invented and Dwight Eisenhower later worked. Now it is part of an €1.8 billion ($2.5 billion) building project at Frankfurt's Goethe University. Not for Goethe's 35,000 students the grotty campuses of others: the "House of Finance" has a marble floor inspired by Raphael's fresco "The School of Athens."

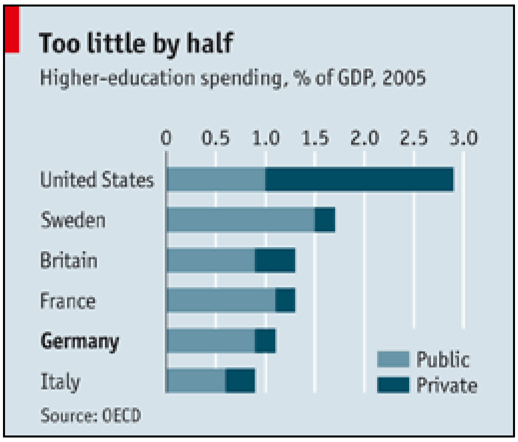
Thousands of less coddled students recently staged protests across Germany against their conditions. "Back education, not banks", demanded protesters fed up with overcrowded lecture halls, crumbling campuses, tuition fees and a chaotic conversion from the traditional diploma to a European two-tier degree system.

German universities are underfunded by international standards (see chart). Professors juggle scores of students; at top American universities they nurture a handful. In switching to the bachelors-masters degrees prescribed by Europe's standardising "Bologna process", many universities tried to cram bachelors degrees into just six terms. Only six German universities are among the top 100 in the Shanghai rankings (Munich is highest, at 55th). Just 21% of each age cohort gets a degree; the OECD average is 37%.

A high-wage country with few natural resources cannot afford sub-par universities, as Chancellor Angela Merkel often says. On June 4th the federal and state governments approved an €18 billion plan to create more university places, boost funding for research and cultivate a small group of elite institutions. It is "a signal that research and education are being taken seriously," says Margret Wintermantel, head of the German Rectors' Conference.

In the past, universities were interchangeable, and most students chose one close to home. But since the early 1990s budget cuts have encouraged them to compete and specialise. Their state paymasters began to link cash to professors' publications and their ability to attract outside money. The government's new "excellence initiative"

goads them to differentiate still more, showering €1.9 billion on research programmes and nine “top universities” with promising “future concepts”. That brought a “big change in mentality”, says Werner Müller-Esterl, Goethe’s president.



Some striking students object to the idea of rewarding research over teaching and of exalting some universities over others. Yet universities are starting to serve students better. All get at least some money based on the numbers they attract. Many go beyond entrance exams to select students. This, plus the introduction of tuition fees and rankings that gauge teaching as well as research, has led to a change in culture with more competition and “a performance orientation,” says Frank Ziegele of CHE, a think-tank that produces a set of rankings.

Goethe University is in the vanguard. Last year it became a “foundation university”, loosening its ties to the state of Hesse, and expanding its freedom to hire and manage staff, and to raise money from private sources. “We can now pay competitive salaries,” says Mr Müller-Esterl. The university has hired 50 new professors, including some from foreign rivals. No longer a state agency, the university now finds it easier to raise money from private donors who want to know how it will be spent. Mr Müller-Esterl hopes the university will build its puny €125m endowment up to €5 billion-6 billion.

But Goethe is not immune to German ailments. Along with other western German universities, it is bracing for an influx of 275,000 extra students, caused by a minor baby boom and a one-year reduction in courses of study at high schools. Part of the government’s package is meant to help universities cope with this “student mountain”, which will peak in 2011-13, but Mr Müller-Esterl says it is not enough.

The main gap in university financing is not the contribution of the state, which matches America’s, but in private funding and fees. Tuition fees, as the student protests suggest, are politically explosive. Hesse’s conservative government introduced them but retreated in the face of protests. That put a check on Goethe University’s leap for independence. Most western German states allow tuition fees of a meagre €500 per term, but universities “can’t plan long term because they don’t know if the next government will take it away,” says Ms Wintermantel.

Nor did universities get extra money for the Bologna process, a source of much angst. The diploma of 8-12 terms was a German brand, “like Oktoberfest,” says Bernhard Kempen, head of the German Association of University Professors. Students who obtain bachelors degrees in some disciplines, such as information technology, do not learn enough to get good jobs. But there is a shortage of places in masters programmes, says Mr Kempen. Students’ mobility among institutions, one of Bologna’s goals, has fallen because study programmes are more intense and universities do not give credit for one another’s coursework. Competition is fine, but professors grumble that they spend too much time on grant applications.

Still, these pressures push German universities in the right direction. World rankings tend to underrate them, partly because non-English-speaking laboratories are penalised. They would do better if research at non-university institutes like the Max Planck Society were brought into academies, adding teaching to research. That is happening: an example is the merger of Karlsruhe University and the Forschungszentrum Karlsruhe to form Karlsruhe Institute of Technology, modelled on MIT. “In ten to 15 years a few universities will have a place in the top international league,” says Matthias Kleiner, head of the Deutsche Forschungsgemeinschaft, which funnels money to research. Perhaps Goethe University will be among them.

France ponders a burqa ban

No cover up

Jun 25th 2009 | PARIS
From The Economist print edition

The government takes on a "walking prison"

WHEN the French government decided in 2004 to ban the Muslim headscarf in state schools and other public buildings, it set off a heated debate over religious expression and women's rights in a secular state. Now Nicolas Sarkozy has sparked another by calling the burqa, a head-to-toe Islamic garment, "a sign of subjugation…of debasement" that is "not welcome on French territory".

Mr Sarkozy's comments came after a group of deputies, led by André Gerin, a Communist, had called for a parliamentary inquiry into the wearing of the burqa, with a view to a possible ban. This would mean in all public places, since it is already banned in state institutions under the 2004 law. The deputies called burqas "veritable walking prisons".

France's strict secularism, entrenched by law since 1905, keeps religion firmly out of the state sphere. There are no religious studies (let alone nativity plays) in state schools, nor may public workers sport the headscarf. The government denies that such policies constrain religious freedom or are especially aimed at Islam. France welcomes private Muslim schools. Mosque-building is widespread. The 2004 headscarf ban outlawed "conspicuous" religious symbols of all faiths. Yet there are growing worries about the spread of hard-line Islamism in the heavily Muslim *banlieues*.

Now that Mr Sarkozy has publicly condemned the burqa, the chances of a ban have risen sharply. Parliament has launched a cross-party mission to report back in six months. In fact, few women wear the full garment in France. But mayors of cities with big Muslim populations report a steady increase in numbers, due not to immigration but to its adoption by French-born women—often from North African countries where the burqa is not traditionally worn.

Rex Features

Not welcome in France

Mohammed Moussaoui, head of the official French Council of the Muslim Faith, has suggested that the inquiry would itself stigmatise Islam. A ban might be misunderstood abroad, and not only in the Muslim world. In his recent speech in Cairo, Barack Obama said that "it is important for Western countries to avoid impeding Muslim citizens from practising religion as they see fit—for instance, by dictating what clothes a Muslim woman should wear."

Not so, say many French politicians—including such prominent Muslims as Fadela Amara, the cities minister. The founder of a women's-rights group, Ms Amara has called the burqa "a coffin that kills individual liberties", and a sign of the "political exploitation of Islam".

Sarkozy addresses parliament

The state of the state

Jun 25th 2009 | PARIS
From The Economist print edition

Reforms relaunched and new ministers, but the same ambiguous president

THIS was to be the moment that Nicolas Sarkozy relaunched his reforms for the second half of his five-year term. On June 22nd, in a ceremony with all the gravitas of an American president's state-of-the-union address, he spoke to a joint sitting of the National Assembly and the Senate in Versailles—the first French president to do this since 1873. Yet, aside from strong words against the burqa (see article), Mr Sarkozy's speech, like his ministerial reshuffle a day later, left unanswered questions.

Typically, Mr Sarkozy offered both more protection and more competition, more borrowing and cost savings, a defence of the French way and a plea for its overhaul. He crowed that "the recession has brought the French model back into fashion." He promised to save jobs and raise unemployment pay. In a phrase bearing the hallmark of Henri Guaino, his market-sceptic speechwriter, he called for new globalisation not based on "each seeking by all means to take jobs and markets from others". Instead of spending cuts or tax rises, he announced a special bond issue.

Yet Mr Sarkozy also said that "the recession powerfully reveals our shortcomings and our weaknesses". He promised reforms of health, education and the civil service, and a public-pension review to consider raising the retirement age. With a budget deficit of over 7% of GDP this year, he promised to squeeze the "bad" part of it, caused by waste and too much red tape, through "courageous reforms".

Ideological gymnastics have long characterised Mr Sarkozy's economic policy. Charitable observers call him pragmatic, pushing what works and dropping what does not. Others say he is craftily pressing ahead with bits of a liberal agenda but keeping the left and the street quiet with social measures. In his reshuffle Mr Sarkozy dealt another symbolic blow to the left by appointing Frédéric Mitterrand, nephew of the former Socialist president, as culture minister.

There was no sign, though, that Mr Sarkozy will tackle France's troubled public finances. A day after his speech Philippe Séguin, the national auditor, declared that "France is approaching a very dangerous zone" and that it was "urgent" to make bigger spending cuts. Christian Noyer, governor of the Bank of France, added that it was "essential" to work out now how to make public finances sustainable.

The reshuffled government, under François Fillon, who remains prime minister, sent mixed messages. The foreign and finance ministers both stay. Pierre Lellouche, an Atlanticist who, unlike Mr Sarkozy, backs Turkish membership of the European Union, is the new Europe minister, replacing Bruno Le Maire, a Germanophile who was meant to improve Franco-German relations (he moves to agriculture). Xavier Darcos, moves on from education, where he gave in to protesters on school reform, to be labour minister.

Mr Sarkozy could now press ahead with his reforms. His ministers have his fresh confidence. His popularity is starting to recover and his party came top in the European election. The opposition is fractured and union-led street protests have fizzled out. In short, the opportunity is there, despite the recession. But his speech gave few signs that he will take it.

Troubled Ireland and Europe

Lisbon's last hope

Jun 25th 2009 | DUBLIN
From The Economist print edition

The Irish government is unpopular—but may still win a Yes to the Lisbon treaty

THE Lisbon treaty has not changed since Irish voters decisively rejected it a year ago. Yet Ireland's prime minister, Brian Cowen, is confident of winning a second referendum on it in early October, despite his government's unpopularity. At the European Union summit on June 18th and 19th the other EU countries gave him enough guarantees over how the treaty will affect Ireland. The first referendum was lost partly because voters were confused by false claims. The guarantees make clear that the treaty does not threaten Ireland's stance on abortion, its right to set corporate-tax rates or its neutrality.

EU leaders have also agreed to change the rules so that each country will now retain a commissioner. The prospect of losing their commissioner (which, ironically, might now happen only if Lisbon fails) seemed particularly to upset voters last June. For Mr Cowen, this is a negotiating triumph—but it is also his sole political success in a dismal year, during which his government has lost public confidence as it struggles to cope with a deep recession.

His poll rating and that of his Fianna Fail-led government are at record lows. Only one in five respondents is satisfied with Mr Cowen's performance; only one in ten with that of the government. Earlier this month Fianna Fail did badly in the European election and worse in local elections, when it recorded the lowest share of the national vote in its 83-year history. Fianna Fail and Mr Cowen have a poor record on EU referendums, losing two out of three since 2001. Yet the polls point to a yes.

That may be because the global downturn has hit Ireland so hard. GDP will contract by 10% this year, say new OECD forecasts, and unemployment may reach 12%. Yet even as the downturn has accelerated, public support for Lisbon has picked up. By last month a two-to-one majority of those who had made their minds up favoured ratification. The recession may have changed voters' minds as they ponder the benefits of membership of the EU and the euro in a financial crisis—and as they note the troubles of a non-member like Iceland.

AP

Cowen, unloved but unbowed

For both sides, the second referendum campaign will be quite different. Given the unpopularity of Mr Cowen's government, success for the yes side will depend on the efforts of opposition parties and non-political groups. The anti-Lisbon side suffered a big setback with the failure by Declan Ganley, founder of Libertas and leading No campaigner last June, to win a seat in the European Parliament and Sinn Fein's loss of its only seat. For Mr Cowen, a referendum success may buy some time. But neither he nor his government can hope to survive another failure.

Silvio Berlusconi's woes

A conqueror, not an end-user

Jun 25th 2009 | ROME
From The Economist print edition

More embarrassment, but the prime minister toughs it out

AN ELECTION win would gladden most politicians. But Silvio Berlusconi, Italy's prime minister, was not inclined to lead the celebrations after his party did well in the second round of local polls on June 21st and 22nd. For on June 18th it had emerged that magistrates in Bari were investigating a possible call-girl ring, and that some of its women had been guests of Mr Berlusconi in Rome.

This has pushed questions about Mr Berlusconi's relations with a young woman from Naples called Noemi Letizia into the background. But it has also meant that he has had to focus more energy on efforts to limit the damage to his reputation than on running Italy or helping its economy.

Mr Berlusconi has turned to his media empire for help. The latest issue of *Chi*, a weekly magazine published by a firm controlled by Fininvest, Mr Berlusconi's family holding company (see article), includes nine pages of photographs and text promoting the prime minister as a family man. In it he denies ever paying women for sex, saying: "I never understood where the satisfaction is when you are missing the pleasure of conquest." Italians have been mostly kept in the dark about the Bari investigation, which has been mentioned only briefly and obliquely on the main television channels. Mr Berlusconi and his children own the three main commercial channels and he exerts strong influence over two of the three owned by the state.

Yet parts of the Roman Catholic Church have now decided that the prime minister is setting a bad example. *Famiglia Cristiana*, an influential weekly, argues that the church cannot ignore Italy's moral emergency. In a strongly worded article the magazine accuses Mr Berlusconi's supporters of defending the indefensible. It attacks Mr Berlusconi's lawyer for describing prostitutes as "goods", and a man who pays them as an "end-user".

Noting that politicians in other countries who transgress moral standards often resign, *Famiglia Cristiana* asks, "why is Italy so different?" Yet Mr Berlusconi is a man of resolve: comparisons with other countries will cut little ice. Nor will calls for him to go be echoed by politicians in his own party—they owe their positions to him. Mr Berlusconi has never enjoyed much standing in international circles. His latest problems will raise a laugh among his guests at the G8 summit next month. But he is unlikely to quit or be driven out.

Charlemagne

A hopper but not a pleaser

Jun 25th 2009
From The Economist print edition

European leaders are grudging in their backing for the European Commission president

Illustration by Peter Schrank

Correction to this article

SOME years ago, when Charlemagne was living in China, he heard complaints that the kangaroo in Beijing Zoo was a very dull animal. The “pouch rat” (as kangaroos are known in Mandarin) just sat there looking miserable, it was said. It did not jump or move at all, no matter how many people prodded it.

Beijing’s kangaroo came to mind at the summit of European Union leaders that ended on June 19th with a provisional decision to grant José Manuel Barroso a second term as president of the European Commission. The EU’s 27 national leaders backed Mr Barroso unanimously, but some were pretty grudging. Their grumbling boiled down to the following thought. Mr Barroso is not much of an inspirational boss for Europe and he seldom takes the lead, no matter how much we prod and humiliate him.

Thanks to pressure from France and Germany, Mr Barroso was not given a legally binding nomination. He must now wait and see if the European Parliament holds a vote on his re-election in July, or drags things out until autumn, a delay that could carry real dangers for him. This came after Mr Barroso endured a strange pantomime of a job interview, at which he presented a programme for the next five years, again at the request of France and Germany. In his letter to leaders, he trawled for German support with talk of a “social market economy” and fostering Europe’s “industrial base”. He reassured Anglo-Saxon types with talk of rejecting protectionism, then wooed the French with a pledge to promote “the development of our agricultural sector”.

At the summit’s end, France’s Nicolas Sarkozy was asked by reporters what he admired about Mr Barroso’s record. With a sour look, Mr Sarkozy ventured that the commission boss contributed to the “success” of the French presidency of the EU in the second half of 2008. He also said that he remembered nothing at all about the first half of the Czech presidency that succeeded it, though he praised the new technocratic prime minister, Jan Fischer, who chaired the summit, for being “calm and intelligent”.

Germany’s chancellor, Angela Merkel, is keener than Mr Sarkozy on Mr Barroso being approved by parliament in July. She called on her fellow leaders to give Mr Barroso a round of applause when he finished his presentation. Yet only hours later, she mocked the commission president while chatting with German

reporters, late on the summit's first night. How Mr Barroso had pestered her for assurances of support, she sighed. She had finally been forced to say to him: "José Manuel, I support you but please leave me alone on this subject now."

Such sniping goes down a treat with Euro-types in Brussels, many of whom are loud in their disdain for Mr Barroso. They yearn for a strong commission boss like Jacques Delors, a Frenchman who bulldozed and outmanoeuvred national leaders into endorsing big leaps forward in EU integration, such as the creation of the internal market and the single currency, during his ten years in charge from 1985 to 1995.

But the same, crucially, is not true of the 27 national leaders of the EU. Put a modern-day equivalent of Mr Delors before an EU summit, and he would not be chosen. As a senior European politician recalled recently, Mr Delors had the near-automatic backing of France and Germany. He also usually had the Benelux countries and Italy on board, as well as newcomers like Spain and Greece. In short, in that far-off Europe of 12 members, Mr Delors's main job was usually to overcome British opposition. Today's Europe of 27 is unrecognisably different. Nowadays, France and Germany disagree as often as they concur on EU policies (their latest dispute concerns budget deficits for euro-area countries: Ms Merkel wants them reduced as soon as the crisis permits, Mr Sarkozy says that deficits are not always bad and insists that "austerity" policies would be a mistake).

The Benelux countries no longer share a vision of Europe. Belgium and Luxembourg remain keen on ever closer union. But Dutch voters are in a terrible mood about the cost of Europe, and the impact of enlargement. Spain remains strongly pro-European, but Italy's political leaders, playing to public fears about immigration and crime, frequently test the limits of EU laws on open borders and free movement. And enlargement to the east has changed Europe forever. If the Lisbon treaty is eventually ratified by all 27 EU members, it will be the last treaty of its type, says a senior figure from the constitutional convention that drafted the first version of what became Lisbon. New members like Poland and the Czech Republic were still candidates for entry during the convention, and so meekly took "orthodox positions", he says. That will not happen again.

Credit where it is due

Given this fragility of the EU at 27, you might think that Mr Barroso would earn more credit for his pragmatism and tireless pursuit of consensus and unity. Even his critics concede that he is a man of acute political instincts. Most, if pushed, will also admit that he is a far more effective administrative boss than his two predecessors, the hapless Jacques Santer and the clever but incoherent Romano Prodi. So why was the mood so glum at the summit as national leaders backed Mr Barroso for another term?

If he does not enthuse some leaders, it is perhaps because Mr Barroso incarnates their bad conscience about their nationally minded behaviour. The more honest know they would not tolerate a commission boss willing to push their government into a corner and outvote them in the name of Europe. The more sensible know that such a chief could break the EU apart. But political leaders are hypocrites like everyone else. They do not enjoy admitting painful truths to themselves, so they transfer their guilt to Mr Barroso. That is unfair, but such is life. Just ask the zoo visitors who blamed the kangaroo for being depressed.

Economist.com/blogs/charlemagne

Correction: we originally named the Czech prime minister Ivan Fischer, when he is in fact Jan Fischer. Sorry. This was corrected on June 26th 2009.

Correction: Eva Joly

Jun 25th 2009
From The Economist print edition

In our analysis of France's European election (June 13th) we described Eva Joly as Franco-Swedish. In fact she is Franco-Norwegian. Sorry

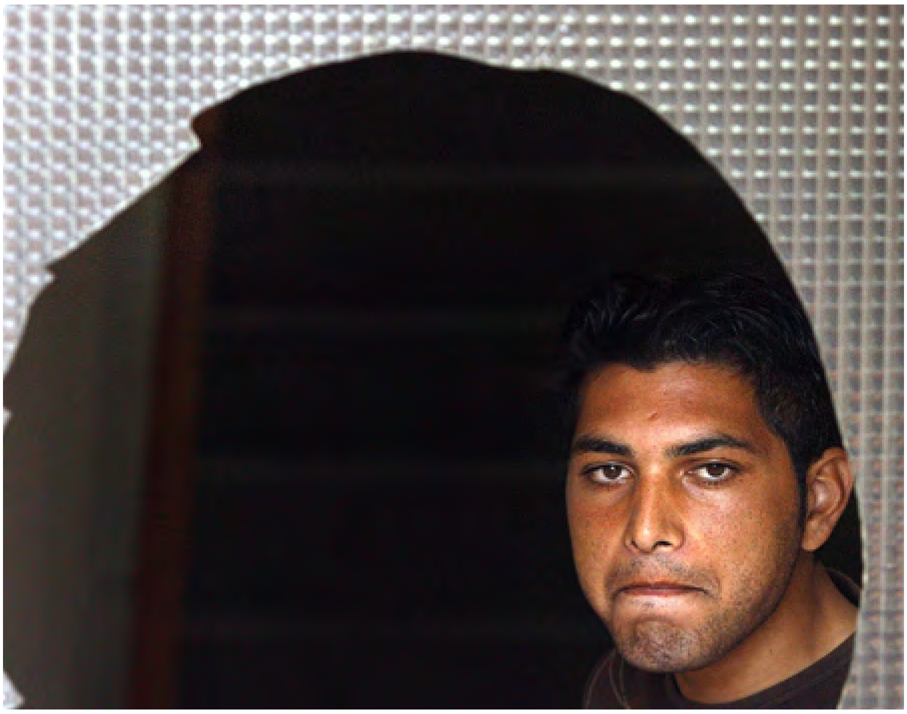
Racism

From the streets to the courts

Jun 25th 2009
From The Economist print edition

A mini-pogrom in Ulster has shocked Britain. But a legal battle with the far right is brewing on the mainland

AP



RACIST bogeymen leered out of newspaper pages in both Britain and Northern Ireland this week. On the mainland, the far-right British National Party (BNP), which won its first two seats in the European Parliament earlier this month, was given an ultimatum by Britain's equality watchdog to step in line with non-discrimination laws or face legal action. Separately, white thugs in Ulster hounded more than a hundred Romanian immigrants—mainly Roma gypsies—out of their homes and, in most cases it now seems, away from the province altogether.

The attacks in south Belfast were of the sort that Northern Ireland hoped had died with the Troubles. Over several nights crowds stoned the homes of immigrant families, smashing windows and posting extracts of *Mein Kampf* through letterboxes. Tension between locals and east European immigrants had simmered since football hooligans clashed at a match between Poland and Northern Ireland in March. When the intimidation reached a peak on June 16th, the Romanians were moved to a church hall and then to a leisure centre. On June 23rd Northern Ireland's government announced that most had decided to return to Romania.

Northern Ireland elected no far-right politicians to the European Parliament in the polling on June 4th. Nonetheless, many in Britain reckon that their neighbours over the water are a more prejudiced bunch than they are themselves. Socially, Ulster leans to the right: civil partnerships, greeted with a shrug by most British Tories, attracted protests in Belfast when they were introduced in 2005; abortion is also more restricted than on the mainland.

It may be that these conservative attitudes extend to scepticism about outsiders. A survey published on June 24th by Northern Ireland's Equality Commission, a statutory watchdog, found that nearly a quarter of the population would be unhappy if a migrant worker moved in next-door. People were even more hostile to Irish travellers, sometimes called gypsies (and often confused with Roma). Just over half said they would mind having travellers living next to them.

Comparing these results with the rest of Britain is hard because surveys produce different answers according to how a question is worded. Across the United Kingdom, less than a tenth of whites say they would mind having a black or Asian boss (though nearly a third admit to being at least “a little” racially prejudiced). But the trends on the mainland and in Ulster are in sharp contrast. British hang-ups about minorities have fallen pretty steadily over the past 20 years, according to the British Social Attitudes Survey, a big questionnaire. By contrast, Northern Irish dislike of travellers is up by a quarter from 2005.

Yet sectarian tensions in Northern Ireland are relatively low. Only 6% now say they would mind having a neighbour of a different faith. One theory goes that the fizzling out of the old disputes has helped to stoke other ones. “The attitudes that facilitate sectarianism may find new outlets in new times,” suggested Bob Collins, the head of the commission. Immigrants are not the only victims: anti-gay sentiment, falling across Britain, has gone up by more than half in Northern Ireland since 2005.

Glass houses

The election of a man with a conviction for inciting race hatred to represent northern England in the European Parliament spoils any pretty notion that all is well on the mainland. But the selection of Nick Griffin, the leader of the BNP, and his colleague Andrew Brons, a former National Front chairman, has provoked a legal challenge from the Equality and Human Rights Commission (EHRC), a mega-watchdog.

The EHRC wrote to Mr Griffin on June 23rd that it believed the BNP fell foul of the law in its race-based membership policy, its hiring (which appears to be restricted to party members) and what the EHRC interpreted as hints that the party would not provide an equal service to constituents of all races. Unless the BNP changes its ways by July 20th, the watchdog will seek a court order to force it to; if the party held that in contempt it could face fines, imprisonment—and publicity.

Why pounce now? First, the EHRC was born only in 2007. Its predecessor, the Commission for Racial Equality, lacked the power to pursue this sort of independent legal challenge. Second, the law has been clarified: the law lords ruled in November 2007 that certain functions of political parties are indeed subject to the Race Relations Act of 1976, which had been in doubt.

Most obviously, the action was triggered by the electoral success of the BNP which, coupled with talk in Westminster about voting reform likely to benefit small parties, has made it harder to dismiss as a sideshow. Others have moved against the BNP since the election: the Royal British Legion, a veterans’ group, publicly called on Mr Griffin to stop wearing its poppy emblem; the government is pondering banning BNP members from teaching, just as they are already banned from the police and prison services. A forthcoming bill on equal opportunities is expected to include a clause explicitly to stop the BNP and its ilk from insisting on race-based membership.

If the EHRC’s complaint goes to court, it will not be the first time a case against a political party has tested race-relations laws. The 1976 act followed a House of Lords ruling in 1973 upholding the right of East Ham South Conservative Club to ban a Sikh because of his race. And the 2007 Lords’ ruling that has clarified the grounds for the EHRC’s current case was over a complaint by a Pakistani man—upheld by their lordships—against the Labour Party.

TIFs and urban development

Regenerating cities

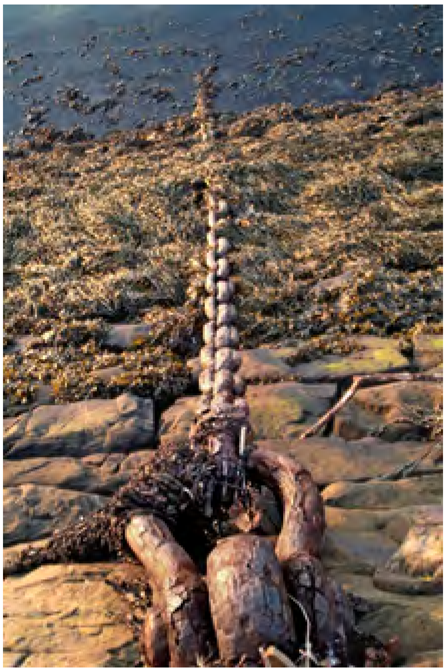
Jun 25th 2009 | EDINBURGH
From The Economist print edition

Britain looks westward for tips on tarting up its towns

ACRES of flourishing weeds adorn derelict docks and warehouses on Edinburgh's northern shoreline by the river Forth. Two years ago city planners were busily drawing up 30-year projects to build 30,000 houses, as well as hotels, offices, shops and parks on the waterfront. Then the credit crunch hit. Now plastic sheeting shrouds a bankrupt developer's half-built luxury flats. Forth Ports, the docks company, has written down the value of much of its extensive landholding to zero.

City bosses, however, think they can get things going again. Their immediate problem is finding the £484m ($799m) they reckon is needed to build roads, schools and other public facilities. In the boom years, local authorities routinely demanded and got a big slice of that money upfront from property developers. These "developer contributions" have now disappeared, and recession means that Edinburgh, like most councils, cannot sell surplus land and property to fill the hole.

Alamy



Tomorrow's shopping centre

The city's solution is to copy a 50-year old American approach: the unlovely sounding tax-increment financing (TIF). The idea is to draw a boundary round an area, borrow to pay for basic infrastructure and repay the loan from the increase in property-tax revenues inside the redeveloped zone as private firms start building.

Edinburgh hopes to test out TIFs on a square kilometre in the suburb of Leith, borrowing £50m to build roads, a dock for mooted cross-river ferries and a new pier for the former royal yacht Britannia, now a tourist attraction moored behind a modest shopping centre. Dave Anderson, the city's development director, hopes that 2,200 houses, plus shops and offices, will follow. PricewaterhouseCoopers, an accounting firm, reckons all this will pull in an extra £280m in business rates (property taxes) over the next 30 years, more than enough to repay the loan.

Scotland's devolved government is keenly interested in these TIF plans and so is Alistair Darling, Britain's chancellor of the exchequer. After he intimated in April that he would entertain the notion of TIFs (business rates are collected nationally and handed back to local governments, so the law would need amending), lots of city councils have come up with ideas for them. Newcastle wants one to build a "science city" geared towards commercialising university research. Leeds hopes a TIF will accelerate growth as it tries to create 20,000 jobs in its Aire Valley business park. Birmingham, thinking big as usual, plans to raise £1 billion for seven road and rail schemes across the West Midlands.

The bravura of this last vision suggests how TIFs can get out of hand. Chicago now has 158 such zones, covering 29% of its land and 13% of its property by value. Mike Jasso of the city's community-development department says that businesses were leaving Chicago's Loop before it became a TIF district in the 1980s; now the zone is thriving. Others are much more sceptical, contending that many successful TIF schemes are in areas that would have attracted investment anyway. Rachel Weber, of the University of Illinois at Chicago, thinks TIFs make Chicago's "dysfunctional system of quid-pro-quo politics more dysfunctional". Every local politician wants a TIF in his district, and developers are eager to contribute to campaigns in the hope of securing support for their projects. In April the city council passed a measure that will, at the very least, increase transparency.

Mr Darling, whose officials will be discussing TIFs with developers and councillors before long, is likely to worry that TIFs are just another way to increase ballooning public debt. Most preliminary studies assume that, because banks and investors are leery of investing in property these days, the loans will have to come

from the government. Having bailed out HBOS, an overextended property lender, just last year, Mr Darling may hesitate to plunge further into that line of business. Recession itself could also prove too big a hurdle: in Chicago, TIF-district tax revenues are slowing, and so is building work. Tempting though it is, borrowing against future revenues may not be the magic wand that Britain's city bosses are hoping for.

Dentists and the NHS

Toothache

Jun 25th 2009
From The Economist print edition

Better than billed, but British teeth are still causing trouble

A DODGY accent and startling false teeth were all that was needed to turn Canadian actor Mike Myers into the British super-spy Austin Powers. In "The Simpsons", a television show, Ralph Wiggum's dentist scares him into brushing with the decaying snaggle-teeth of the (fictional) "Big Book of British Smiles". And there is some truth behind the awful stereotype: the factory workers of Britain's Industrial Revolution were fed on sugar from the colonies, and led the known world in dental caries. Early in the 20th century Americans were brushing and flossing while some British dentists still believed that chomping on hard foods kept teeth strong. As recently as 1968, well over a third of British adults had not a single natural tooth in their heads.

So it is hardly surprising that, since its founding in 1948, the National Health Service has struggled to cope with the dental needs of the population. During its first two years it supplied 100m false teeth, and the first patient charges it introduced, in 1951, were for dentures. The legacy of bad teeth is still putting NHS budgets under strain. In recent years many dentists have turned to private practice as fees for doing NHS work have been squeezed.

Alamy

The way we were

On June 22nd came the latest attempt to fix NHS dentistry: an independent government-commissioned review, the third on the subject in 18 years. Changes in 2006 had been intended to simplify payments for NHS work, and to encourage dentists to concentrate less on drilling and filling and more on prevention. Instead they had unintentionally rewarded dentists for over-treating fewer patients, and forced more than ever to suffer or go private. This week's review recommends re-complicating rates a bit, and once again paying dentists partly according to the number of NHS patients on their books. It is quite a U-turn.

How could the 2006 reforms have missed the mark so widely? By not being piloted, for one thing: the review team wants its prescriptions tested in a few areas before they are applied nationwide. A less tractable problem is that the evidence about what works is weak. Crowns and fillings are a success only if they last; trials must run for many years, by which time new materials and methods are in use.

"That means wide variations in practice, and lots of wiggle-room for dentists to respond to financial incentives," says the review's lead author, Jimmy Steele, a professor of dentistry at Newcastle University. And respond to the 2006 changes dentists did, doing fewer tricky root canals and more extractions, referring more acute cases to dental hospitals and halving the treatments involving laboratory work.

More generally, the gap between the necessary and the cosmetic is wider in dentistry than other areas of medicine, making it hard to agree on what the state should subsidise. Bridges or implants? How crooked is too crooked? How stained is too stained? The value placed on saving a tooth varies wildly from person to person, the review team found, from nothing at all to as much as £10,000 ($16,500) for a molar. Generations differ, too. Few of Britain's "heavy metal generation"—the 45-75-year-olds with mouths full of amalgam—aspire to Hollywood-style teeth, because they look far too similar to their parents' and grandparents' dentures. Should their taxes go towards capping and bleaching the teeth of youngsters who rather fancy the perfectly even, blue-white look?

As for advising on prevention, which is probably the most important part of modern dentistry, there is a problem. Britons who visit the dentist feel cheated if all they get is a quick peer and a reminder to floss. But that may change, and surprisingly quickly. Probably because treatment is easily available to children on the

NHS, Britain is one of a handful of OECD countries where 12-year-olds have fewer than one decayed, filled or missing tooth per head. (In Europe, only Danish and German children do as well.) British teeth could soon be dazzling the world.

The Conservatives in the EU

Eurochums

Jun 25th 2009 | BRUSSELS
From The Economist print edition

The Tories' new allies are a motley crew

NOT fascists, but not obvious soul mates either: that is a fair summary of the politicians invited on June 22nd to join Britain's Conservatives in a new grouping in the European Parliament. Most are nationalists or social conservatives whose views hardly chime with the moderate messages pushed by David Cameron at home. How did this happen?

Mr Cameron promised, during his campaign to become Tory leader, to leave the main centre-right grouping, the European People's Party (EPP), and found a new one committed to free trade and opposition to a federal Europe. In these cynical times, it is tempting to cheer him merely for keeping his word.

The new "European Conservatives and Reformists Group" consists of 56 MEPs from nine countries, 26 of them British Conservatives. Tories say that staying in the EPP was inconsistent with campaigning at home to defend British sovereignty. They have a point: the EPP is dominated by federalists. They are also right that no grouping is entirely wholesome. The socialist group, in which Britain's Labour Party sits, heaves with ex-communists from the east. The EPP, for its part, is home to post-fascists from Italy.

The Tories point out that their key allies, Law and Justice in Poland (with 15 MEPs) and the Czech Civic Democrats (with nine), were until recently parties of government. They scoff, with reason, at suggestions that Mr Cameron would be ostracised by EPP stalwarts such as Nicolas Sarkozy of France or Angela Merkel of Germany were he to become prime minister. And perhaps their more exotic allies were forced on the Tories by rules that require at least 25 MEPs from seven countries to form a parliamentary group entitled to extra funding and access to senior parliamentary posts.

But critics also have a point. The Tories did not control who sat with them in the EPP; in founding a new group, they invite closer scrutiny of their allies. That scrutiny reveals a muddled picture. Mr Cameron has managed to avoid the extreme right, but he has broken with large mainstream parties.

In Poland, the governing centre-right party is the Civic Platform. To the far right sit fringe politicians with openly anti-Semitic views. Mr Cameron's allies are in the middle, with wrong-headed opinions on gays and capital punishment. In Belgium, the Christian Democrats belong to the EPP. Mr Cameron has nothing to do with the anti-immigrant parties on the far right, but his allies are from the Lijst Dedecker, a populist outfit that wants independence for Dutch-speaking Flanders. In the Netherlands too, the largest party, the Christian Democrats, is in the EPP. Mr Cameron has eschewed the anti-Islamist Geert Wilders but his partners are from the tiny Christian Union, which favours government guided by biblical commandments. And the Tories' sole Latvian chum is a mild-mannered economist, a wing of whose party annually honours Latvians who fought with the Waffen SS against Soviet forces.

Mr Cameron's real problem is structural. Europe makes even centrist voters cross in Britain, yet centrists on the continent are overwhelmingly pro-EU. So to find allies who share their Euroscepticism, Tories have to seek out populists and angry nationalists. Mr Cameron's new band of allies may be a symptom of Britain's strained relationship with Europe rather than a solution to it.

MPs choose a new figurehead

Laws, sausages, speakers

Jun 25th 2009
From The Economist print edition

It's best not to know how John Bercow was elected

Reuters

THE determination of the House of Commons to spurn any opportunity to rebuild its good name is something to behold. The expenses scandal that disgraced it could have been contained by full disclosure of MPs' claims as soon as a newspaper began publishing the leaked information in May. Instead, the Commons authorities waited until June 18th to release the receipts, and they were heavily redacted.

The second missed chance for redemption occurred on June 22nd. The election of a new speaker of the Commons to replace Michael Martin, who was forced to step down after seeming indulgent of parliamentary nest-feathering, could have showcased Parliament at its most high-minded. It did nothing of the sort.

The problem was not so much the winner, John Bercow, though many accuse him of self-promotion, travelling lightly when it comes to fixed beliefs and making merry with taxpayers' money himself. His clear and fluent speaking style has already distinguished him from Mr Martin, whose thickly accented mumble rarely commanded raucous MPs. At 46 a generation younger than Sir George Young, his main rival for the job and a fellow Conservative, he can claim to be the modern candidate. The son of a taxi driver also continues the recent trend of MPs from humble backgrounds filling one of the most gilded posts in British public life.

Yet the manner of his election saw MPs at their most tactical and partisan. Labour MPs backed Mr Bercow simply to annoy the Tories, who are cynical about his journey from strident Thatcherism to metropolitan liberalism. (Rumours that he was about to defect to the Labour ranks have dogged Mr Bercow several times in recent years.) Meanwhile, the Tories' hostility towards him betrayed an intolerance of dissent, with some hotheads privately pledging to depose Mr Bercow if, as expected, the Tories win the next general election. The need to salvage Parliament's reputation—the very reason for ditching Mr Martin—gave way to the rankest tribalism when it came to choosing his successor.

The common sense of senior Tories should spare Mr Bercow from a putsch but he will be watched more closely than any recent speaker. He wants to clean up Parliament, make it more independent of the executive and promote the virtues of the House of Commons to a cynical public. Some are dubious about the last of these missions, suspecting Mr Bercow of characteristically seeking the limelight. But it may be the only one of the three that he can do much to advance. The capacity to reform politics resides largely with the government. The day after Mr Bercow took the speaker's chair, Harriet Harman, the leader of the Commons, announced legislation that would establish an independent body to monitor MPs and create jail sentences for some violations of expenses rules.

By contrast, Mr Bercow's power to reform does not extend much beyond overseeing the Commons fees office, standing up for backbenchers and the opposition in debates, and using the speaker's chair as a bully pulpit. Persuading voters that MPs are not so bad is a task that MPs themselves may be better placed to

undertake. It is a tradition for a newly elected speaker to be dragged to the chair reluctantly. Though Mr Bercow campaigned for his new job, he might have done better to resist.

Wildcat strikes

Lockout

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Fire and brimstone at a Lincolnshire sulphur plant

TROUBLE at a Lincolnshire oil refinery has triggered wildcat strikes, now in their second week, at engineering sites across the country. Discontent in the industry runs deep, and not only because of recession. An ill-applied European Union (EU) directive, say trade unionists, has destabilised the national employment agreement that has governed the engineering construction industry in Britain since Margaret Thatcher's time as prime minister.

Tempers flared at the Lindsey plant because 51 contract workers handed their notices on June 10th reckoned they should have been given the chance to apply for 61 new jobs that had been filled two days earlier. Their fellow workers, building a desulphurisation plant at the refinery, downed tools on June 11th. A week later 647 of them were fired, prompting sympathy strikes by around 3,000 workers at a score of other sites. Many of those dismissed at Lindsey had gone on strike in February, in protest against an Italian subcontractor that imported its entire workforce, doing locals out of the chance of a job.

AFP

And one for all

Large construction sites such as Lindsey rely on a raft of subcontractors, each hiring workers on its own terms. Total, the French oil company that owns the refinery, says delays and low productivity there have cost it an extra £100m so far but claims to be at arm's length from the dispute. It still attended talks between unions, contractors and the National Joint Council for the Engineering Construction Industry, an employers' group, in London on June 23rd.

Even if this squall is calmed (talks were due to resume as *The Economist* went to press), that will not resolve the mismatch between the National Agreement for the Engineering Construction Industry (NAECI) and the application in Britain of the EU's Posted Workers Directive (PWD). Suspicions abound that foreign subcontractors, working on British sites, bring in foreign workers with pay and qualifications that are below NAECI standards. GMB, a trade union, unmasked such a case in March, it says: a Polish worker at a site in Kent was being paid £4 an hour less than the NAECI minimum.

The PWD itself sets minimum standards, but they are not supposed to undercut national ones. Recent judgments by the European Court of Justice, though, have held that strikes to demand conditions better than those the PWD sets out are not justified. Britain's new Department for Business, Innovation and Skills has noted the implications, says a spokesman, and is taking part in EU revisions.

Meanwhile, there is a face-off between the ECIA and the unions over the national agreement, which must be renegotiated by the end of the year. The employers want a wage freeze in January. The unions naturally disagree. But they also want more transparency from contractors on what they intend to pay workers when bidding for British contracts. Lack of such transparency was one shortcoming identified by a report after the first Lindsay strike, by the government-sponsored Advisory, Conciliation and Arbitration Service.

Early in June GMB and Unite, two big unions, said they would poll around 25,000 workers at 100-odd sites on whether the impasse justified strike action. The ballot is taking time to organise, concedes a GMB spokesman. Frustratingly for the unions, perhaps, a national strike at engineering construction sites would not cripple the country, for it would not affect the running of power stations and refineries themselves. The contract workers, never part of a permanent workforce, do not have much clout, and their national

agreement may be an anachronism. Many industries, according to a new survey by the Confederation of British Industry, have seen surprising co-operation between employers and their workers as they combat recession, agreeing flexible hours and wage freezes rather than redundancies. A rigid national agreement may not be the best way to lure foreign investors like Total to Britain, or to save local jobs.

Setanta goes bust

Heroic failure

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From The Economist print edition

A sports broadcaster's demise should trouble regulators as much as fans

Reuters

All right for some

IN IRISH folklore Setanta was a mighty hero, as skilled and fearsome with hurley and ball as with the sword—until he met evisceration and a bloody end. The modern Setanta, a sports broadcaster founded by two Irish businessmen in 1992, never quite matched the myth, except perhaps in death. Its British business (its biggest) went into administration on June 23rd, having been gutted as fatally as its legendary namesake. About 200 people have lost their jobs. Its Irish and international parts are still going, but they are for sale.

The mortal wound was the loss of Setanta's main attraction—46 English Premier League football matches next season, plus 23 in each of the next three—triggered by its failure to keep up payments. The league resold the rights on June 22nd to ESPN, a sports broadcaster owned by Disney (which had been outbid by Setanta before). Though familiar in America and many other places, ESPN is much less well known in Britain.

The other bodies with which Setanta had deals are either seeking new broadcasters or expected to do so. These include the Scottish Premier League (SPL), the Football Association, non-league football and England's leading rugby clubs, and some foreign rights-holders. Some will be hurt more than others—and the Premier League not at all. ESPN is reported to have offered the same sum, £159m, that Setanta bid for 2010-13. It is thought to have paid a good deal less than the £130m Setanta offered for next season's games, but down-payments by Setanta should fill the gap. In any case, most games belong to—and most money comes from—BSkyB, Britain's leading pay-TV provider.

In non-league and Scottish football, though the amounts are much smaller, Setanta's loss is more worrying. It had a four-year, £54.5m deal with the SPL running until 2010 and a new, £125m contract lasting until 2014. The SPL recalled its rights on June 22nd and needs a new contract sharpish. According to a report by PricewaterhouseCoopers, an accounting firm, almost every SPL club made a profit, or nearly did, in 2007-08. But at some, up to 30% of income comes from Setanta. "Without this income", says the firm, "drastic cost reductions will be required and some clubs might not be able to survive this process."

Setanta's failure is also a problem for regulators, who have tried to stir competition for top-flight football rights in the hope of creating rivalry for BSkyB. Setanta secured Premier League games in the first place only because of an agreement between the league and the European Commission. This said that BSkyb, which had screened all the games on offer since the league's inception in 1992, should not be allowed the lot. It could have at most five out of six batches of 23, starting in 2007.

This hasn't done much good. Consumers are worse off: fans wanting all the televised games had to buy Setanta's as well as BSkyB's, and so had to pay more than before. Setanta was always a marginal, weak competitor. It lacked a satellite or cable "platform" on which to deliver programmes—yet tried anyway to sell directly to customers, with all the costs that entailed. It attracted only 1.2m subscribers, most of those through BSkyB's satellites, and a lot of complaints. Enders Analysis, a consulting firm, reckons it needed 1.9m. The only gainer was the Premier League, which did very nicely from the auctions.

BSkyB looks no less powerful than before. Ofcom, the British broadcasting regulator, is due to publish a report on the pay-TV market by the end of the month. At issue are the terms on which those who have programmes sell them to those with platforms—in particular, the terms of BskyB, which has both. And it has the football that people will pay to watch.

Bagehot

The last judgment

Jun 25th 2009
From The Economist print edition

What the new inquiry into the Iraq war can and can't achieve

Illustration by Steve O'Brien

AT THE end of "The Italian Job", do Michael Caine and his gang survive? What was Jack the Ripper's real identity? Was Britain's involvement in Iraq an absolute debacle, and if so, who was responsible? Wherefore do the wicked prosper?

Which of those is the odd one out? Actually, that was a trick question: none of them is. The question about Iraq shares a quality with the others. It will never be answered definitively and to universal satisfaction—including by the new inquiry cack-handedly announced by Gordon Brown. But that limitation does not mean, as some carpers argue, that it is mistake to hold it at all.

Britain should be prepared for what the inquiry under Sir John Chilcot, a retired civil servant, is unlikely to achieve. Even without Mr Brown's stipulation that it wouldn't "apportion blame" (later finessed by David Miliband, the foreign secretary), it probably wouldn't have done. Such probes, whether into foreign entanglements or agricultural blight, tend not to blame anybody very much. They are conducted by bigwigs in suits; they interview other besuited bigwigs, typically find them well-meaning and conclude that any shortcomings were inadvertent or systemic. This is not always because the inquiries are stitch-ups; caste and unconscious sympathy also contribute.

As the carpers point out, there have already been assorted Iraq reviews in Britain, both independent and parliamentary. There have been more in America, congressional and otherwise, and elsewhere. Journalists have written books and memoirs, as have participants in the fighting and the pre-war diplomacy. Previous British reports, which concentrated on the government's use of intelligence, have been dismissed as whitewashes.

In fact, on that most controversial and intricate of questions, much that is shaming and scandalous is already known. The omission of caveats and subjunctives; the extrapolations from thin and dated intelligence; the infamously misrepresented "45-minute" claim; the blinkered misreading of crucial evidence

on Iraq's nuclear programme: the whole shoddy repertoire of mistakes and techniques that made a hunch about Saddam Hussein seem urgent is painfully well documented. It was partly documented by a committee under Lord Butler, of which Sir John was a member, though its criticisms were swaddled in blandly conciliatory prose and so derided. Whether Tony Blair or others "lied" about the Iraqi threat may remain known only to them; more a theological issue than one soluble by Sir John.

It is likewise doubtful that there will be further revelations concerning the government's motive, and the related matter of timing—that is, when exactly Mr Blair committed Britain to participating in the war. Maybe freshly available cabinet documents or diplomatic traffic will shed new light. But when he gives his evidence, Mr Blair will surely regurgitate his familiar messianic-Manichean *shtick*, plus his view that American power is best steered by working alongside it. It can be hard for anyone to recollect his motives at a distance; memory often sanitises and ennobles, even in much more trivial cases than the launching of a devastating war. Mr Blair is not likely to say, "OK guys, you got me—I did it out of lust for glory and infatuation with George Bush."

Act in haste, redact at leisure

Those are causes for scepticism. But there are others for thinking the inquiry necessary. Iraq has sorely strained the covenant between the armed forces and the country they defend. It has left deep grievances among ordinary soldiers and top brass about funding, equipment and manning levels, some of them voiced by General Sir Richard Dannatt, the outgoing head of the army, this week. Even though several of these worries, too, have already been investigated, Sir John's panel could offer a valuable overall verdict on whether Mr Blair's government put Britain's money where his mouth was, and if not, why not. That may have cautionary implications for defence strategy more broadly.

Then there are the errors and missed opportunities of the reconstruction effort, some of which General Dannatt also discussed. Why, before the war, were the conditions in Iraq after it so catastrophically misjudged? An analysis of those failures—and of how far British politicians and commanders were prisoners of policies dreamed up in the Pentagon—might inform future decisions on whether and when to go to war as a junior partner.

Perhaps most importantly, if intangibly, there is that other fractured covenant, between government and the people. The Iraq war is a great national welt of grief, shame and mistrust. Some of the damage—the deaths, most obviously, but also the impact on Britain's international standing and security, and on the Labour Party's moral authority—cannot be salved by Sir John. But in a ceremonial, almost primitive way, some of the rancour might be lessened, if the process is overwhelmingly conducted in public. That now seems probable, despite Mr Brown's initial, indefensible preference for a closed version: with Mr Bush departed and Saddam dead, the case for privacy was always piffling. One of the other criticisms of Mr Brown's botched proposal, however—that the inquiry should take less than the year he suggested, and report before the general election—is mistaken. It will take at least a year for it to do a thorough, therapeutic job.

In 2003 one of the firmest grounds for thinking Saddam was up to no good was that he acted guilty, even when the invasion was on his doorstep. In 2009 one good reason to favour an inquiry is that Mr Brown has behaved so shiftily over it. (What happened in Iraq should stain his record, and his conscience, almost as much as Mr Blair's, for all he might like it to be or seem otherwise: he may have been the only other individual who could have kept Britain out.) It may not, in the end, find the current or former prime minister guilty. But it is still a vital undertaking.

Economist.com/blogs/bagehot

Migration and climate change

A new (under) class of travellers

Jun 25th 2009 | ADDIS ABABA AND LOKICHOGGIO
From The Economist print edition

Victims of a warming world may be caught in a bureaucratic limbo unless things are done to ease—and better still, pre-empt—their travails

Panos

THE airstrip at Lokichoggio, in the scorched wastes of north Kenya, was once ground zero for food aid. During Sudan's civil war, flights from here kept millions of people alive. The warehouses are quieter now, but NGOs keep a toehold, in case war restarts—and to deal with what pundits call the "permanent emergency" of "environmentally induced" migration.

Take the local Turkana people. Their numbers have surged in recent decades, and will double again before 2040. But as the area gets hotter and drier, it has less water, grazing and firewood. The drought cycle in northern Kenya has gone from once every eight years to every three years and may contract further. That means no recovery time for the Turkana and their livestock; the result is an increasingly frantic drift from one dry place to another.

A local crisis with local causes? Only partly. Scientists think it is part of a global phenomenon: people across the world on the move as a result of environmental degradation. Just how many are moving, or about to move, is maddeningly unclear.

The International Organisation for Migration thinks there will be 200m climate-change migrants by 2050, when the world's population is set to peak at 9 billion. Others put the total at 700m.

These startling numbers may conjure up a picture of huge, desperate masses, trekking long distances and if necessary overrunning border defences because their homelands have dried up or been submerged. But at least initially, the situation in Kenya and other parts of east Africa is likely to be more typical: an already poor population whose perpetual search for adequate pasture and shelter grows harder and harder. In such conditions, local disputes—even relatively petty ones between clans and extended families—can easily worsen, and become embroiled in broader religious or political fights. And that in turn makes it harder for everybody in the area to survive, and more desperate to find new places to live, even if they are not far

away.

A new report—"In Search of Shelter"—by the United Nations University, the charity CARE and Columbia University in New York lists the eco-migration "hot spots": dry bits of Africa; river systems in Asia; the interior and coast of Mexico and the Caribbean; and low islands in the Indian and Pacific Oceans.

A one-metre rise in sea levels could displace 24m people along the Ganges, Brahmaputra, Irrawaddy, Salween, Mekong, Yangtze and Yellow rivers—which together support a quarter of humanity. A two-metre rise could uproot 14m people on the Mekong alone and swamp much of its farmland. Meanwhile, the melting of the Himalayan glacier will cause floods and erosion upstream, boosting the price of rice and other staples. And many regional conflicts could be exacerbated.

The scale of the likely population shift raises big questions. Will climate-change migrants be recognised? The classic definition of refugees—tossed between states by war or tyranny—is outdated. Eco-migrants will be paperless paupers, whose multiple woes are hard to disentangle.

Poverty campaigners want a revised legal regime to protect the new migrants. However, this looks tricky. America resists calling them "environmental refugees": the word "refugee" implies guarantees that cannot realistically be given to the coming torrent of migrants. As American diplomats quietly admit, their rich country is still reeling from Hurricane Katrina in 2005, which killed 1,800 people and displaced hundreds of thousands.

Can the United Nations High Commissioner for Refugees (UNHCR) expand to cope with eco-migrants? It has already struggled to widen its remit to include the internally displaced (26m at the end of 2008) as well as strictly-defined refugees (10m, excluding the Palestinians who come under another agency). A tenfold surge in the numbers within its orbit would push the agency out of control, says James Milner, a professor at Ottawa's Carleton University. Meanwhile some aid workers see signs of a competition between institutions to take ownership of the eco-migration issue, perhaps by oversimplifying it.

Charles Ehrhart of CARE thinks UNHCR will remain central, but wonders how it or anybody can now distinguish between "forced" and "voluntary" migration. He says climate change may cut agricultural output by half in lowland Africa by 2020. "In such a context, does migration constitute a choice or a necessity?"

Migrants' rights may be easy to assert for islanders whose homes are drowned—but hard in the case of big, messy movements across Africa and Asia. Most of the displaced will drift to the next-most-liveable place, as the poor do anyway.

"Many states are already overwhelmed by internally displaced populations," says Mr Ehrhart. "Will they be able to support even more people on the move? If not, whose duty is it to make up the difference?". At the least, the gap between carbon usage and climate change's effects portends angry North-South rows.

Meles Zenawi, who as Ethiopia's prime minister will speak for Africa at several global gatherings this year, predicts that some parts of the continent will become uninhabitable and "those who did the damage will have to pay." At the December summit on climate change in Copenhagen, he hopes that Africa will "aggressively" demand compensation for environmental damage as well as help with migrants and the mitigation of climate change: in his view a demand of $40 billion would be reasonable.

Many agree that more research is needed to pinpoint the reasons why migrants pick up sticks. People concur that climate change fuels conflict in Darfur, but nobody knows how big a factor it is. Drought helped jihadist fighters seize bits of south Somalia, but was it the main reason?

Gloom abounds. James Lovelock, an environmental guru, posits a collapse in human population, in part related to migration, with a few "lifeboat" regions surviving. Then there is the pace of social change. The number of "megacities"—with populations in the tens of millions—may grow to several hundred by the middle of the 21st century. Most are poorly planned.

Would a migrant from a collapsed city receive aid? "We've not experienced anything of this kind, where whole regions, whole countries, may well become unviable," says Jeffrey Sachs, head of Columbia University's Earth Institute.

No wonder strategists see vast new security risks, and a big expansion in the world's "ungoverned spaces". But much can be done before the exodus turns biblical. In West Africa subsistence farming is badly

irrigated. Improve that, throw in some seeds and fertiliser, scrap tariffs, build warehouses and roads, and the region may beat the worst of climate change.

Geographers at UN Habitat, a city-planning agency, say conurbations must adapt to the needs of climate-change migrants. “You can’t just stockpile people,” says Alex de Sherbinin of Columbia University. The pressure is tangible in Addis Ababa, which already has teeming slums. The price of teff, a staple, has surged after a famine that is still pushing people to the city. Mr Meles is not alone in his wrath.

The World Bank and the environment

When the learning curve is long

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After an abrupt about-face, an agency frets about its footprint

Still Pictures

Brazil's burning desire for pasture

IF ANYONE suggested the World Bank did not take global warming seriously, its bosses would bristle: only last October, they would point out, the institution issued a "strategic framework" laying out its thinking on development and climate change. This promised more emphasis on noble things like energy efficiency and renewable power; and more bank support for "sustainable forest management, including reduced deforestation."

Those words intrigued green campaigners, who were up in arms over a $90m loan by the bank's private-sector arm, the International Finance Corporation (IFC), to the Bertin group, Brazil's leading beef exporter. As the greens observed, cattle farming is widely seen as the biggest threat to the Amazon's trees.

Doubts about the loan were not confined to angry tree-huggers. In a paper that was initially confidential but leaked on the internet, the bank's own Independent Evaluation Group (IEG)—which is supposed to watch the secondary effects of the agency's work—had argued that the credit posed "a grave risk to the environment".

The IFC overruled this advice, saying in January 2008 that its loan to Bertin would help the firm "in establishing sustainable operations throughout its supply chain, especially with its cattle suppliers in the Amazon region." But on June 12th there was a change of heart. The bank said it was pulling out of the Bertin project: it was no longer satisfied that its concerns over sustainability were being met.

There were yelps of glee from greens—along with harder questions about how possible it really is for the world's leading development agency to promote growth, satisfy its member governments and protect the planet all at the same time.

Defenders of the bank say that its concerns over climate change are more than verbiage: of the $7.5 billion it lent for energy projects in 2008, a respectable $2.7 billion went to efforts aimed at saving energy or boosting renewable power. This was twice as much as it had lent for such projects in 2007. Admittedly, the bank does also fund coal-fired projects, but it insists that wherever possible, it will opt for greener forms of power.

Earlier this year, a (public) report by the IEG said the bank could congratulate itself on promoting energy efficiency. But as it recognised, this success did not mean everyone's heart had turned green: rising fuel prices had made energy saving an easy sell in many countries. And this benign atmosphere may not last. There are poor countries that see environmentalism as a luxury that hurts their immediate growth prospects. On June 22nd Ethiopia blamed power cuts on the World Bank's refusal to fund a 60MW diesel generator.

David Wheeler, a former World Bank economist who is now at the Centre for Global Development, a think-tank, says such tensions are bound to persist. The bank's regional units are under pressure to meet lending targets and get money out to governments. In that culture, the bank's bureaucrats won't work too hard on goals that hold little appeal for client countries.

Still, when countries want to act over climate change, the bank can do a lot to assist. Mexico, for example, has sought help with cutting energy use in city transport and producing cleaner power. The bank is lending

it $500m in low-interest credits out of a $5.2 billion Clean Technology Fund to finance new bus networks, replacing the gas-guzzlers that clog Mexico's roads.

Vinod Thomas, the IEG's director-general, sums up the dilemma: "Climate change threatens to derail development, while business-as-usual development threatens to destabilise the climate."

Managing this tension will involve a lot more reflection about the trade-off between growth, the mitigation of climate change and adaptation to its effects. At the bank, some thinking does seem to be going on: that is the topic of its next World Development Report—an annual assessment of the fight against poverty.

Whatever the report says, it will be hard to convince poor countries that action over climate change is a necessity, not a luxury, and that it will not impede growth. The Bertin shambles may go down as a warning for everybody involved in a giant exercise in on-the-job learning.

A slow-burning fuse

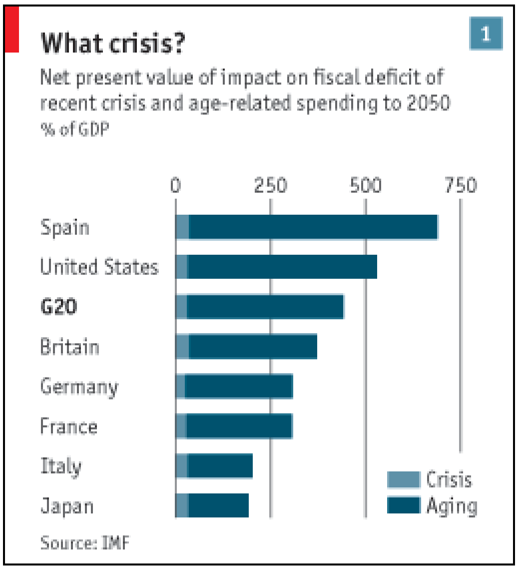
Jun 25th 2009

Age is creeping up on the world, and any moment now it will begin to show. The consequences will be scary, says Barbara Beck (interviewed here)

Corbis

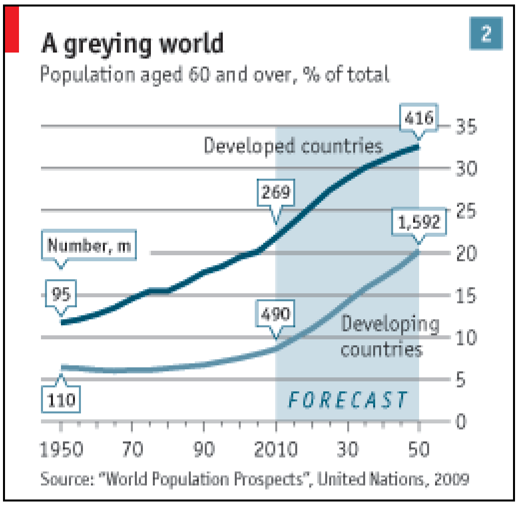
STOP thinking for a moment about deep recession, trillion-dollar rescue packages and mounting job losses. Instead, contemplate the prospect of slow growth and low productivity, rising public spending and labour shortages. These are the problems of ageing populations, and if they sound comparatively mild, think again. When the IMF earlier this month calculated the impact of the recent financial crisis, it found that the costs will indeed be huge: the fiscal balances of the G20 advanced countries are likely to deteriorate by eight percentage points of GDP in 2008-09. But the IMF also noted that in the longer term these costs will be dwarfed by age-related spending. Looking ahead to the period between now and 2050, it predicted that “for advanced countries, the fiscal burden of the crisis [will be] about 10% of the ageing-related costs” (see chart 1). The other 90% will be extra spending on pensions, health and long-term care.

The rich world’s population is ageing fast, and the poor world is only a few decades behind. According to the UN’s latest biennial population forecast, the median age for all countries is due to rise from 29 now to 38 by 2050. At present just under 11% of the world’s 6.9 billion people are over 60. Taking the UN’s central forecast, by 2050 that share will have risen to 22% (of a population of over 9 billion), and in the developed countries to 33% (see chart 2). To put it another way, in the rich world one person in three will be a pensioner; nearly one in ten will be over 80.



This is a slow-moving but relentless development that in time will have vast economic, social and political consequences. As yet, only a few countries with already-old populations are starting to notice the effects. But labour forces are now beginning to shrink and numbers of pensioners are starting to rise. By about 2020 ageing will be plain for all to see. And there is no escape: barring huge natural or man-made disasters, demographic changes are much more certain than other long-term predictions (for example, of climate change). Every one of the 2 billion people who will be over 60 in 2050 has already been born.

The reasons why



What is making the world so much older? There are two long-term causes and a temporary blip that will continue to show up in the figures for the next few decades. The first of the big causes is that people everywhere are living far longer than they used to. This trend started with the industrial revolution and has been slowly gathering pace. In 1900 average life expectancy at birth for the world as a whole was only around 30 years, and in rich countries under 50. The figures now are 67 and 78 respectively, and still rising. For all the talk about the coming old-age crisis, that is surely something to be grateful for—especially since older people these days also seem to remain healthy, fit and active for much longer.

A second, and bigger, cause of the ageing of societies is that people everywhere are having far fewer children, so the younger age groups are much too small to counterbalance the growing number of older people. This trend emerged later than the one for longer lives, first in developed countries and now in poor countries too. In the early 1970s women across the world were still, on average, having 4.3 children each. The current global average is 2.6, and in rich countries only 1.6. The UN predicts that by 2050 the global figure will have dropped to just two, so by mid-century the world's population will begin to level out. The numbers in some developed countries have already started shrinking. Depending on your point of view, that may or may not be a good thing, but, as this special report will argue, it will certainly turn the world into a different place.

The temporary blip that has magnified the effects of lower fertility and greater longevity is the baby-boom that arrived in most rich countries after the second world war. The timing varied slightly from place to place, but in America—where the effect was strongest—it covered roughly the 20 years from 1945, a period when nearly 80m Americans were born. The first of them are now coming up to retirement. For the next 20 years those baby-boomers will be swelling the ranks of pensioners, which will lead to a rapid drop in the working population all over the rich world.

As always, the averages mask considerable diversity. In the richer parts of Asia the populations of Japan, South Korea and Taiwan are already old and will rapidly get even older. Europe is split several ways: Germany, Italy and Spain, for instance, now have tiny families and are therefore ageing fast, whereas France, Britain and most of the Nordic countries have more children to keep them younger. In eastern Europe, and particularly in Russia, birth rates are low and life expectancy has also taken a knock. America, thanks to a resilient birth rate and high immigration, will still be fairly youthful by mid-century.

Most developing countries do not have to worry about ageing—yet. Although birth rates have dropped, populations are still young and will remain so for a few decades yet, even though HIV/AIDS has killed off many active adults. But in the longer term the same factors as in the rich world—fewer births, longer lives—will cause poorer countries to age too. And even before that happens, the absolute numbers of older people there will swell alarmingly, simply because these countries are so populous. They already have 490m over-60s, and that total is due to more than triple by 2050. Since most poor countries have little or nothing in the way of a state-funded welfare net, those numbers will be hard to manage.

Alone among developing countries, China is already ageing fast. This is mainly because for the past 30 years it has been keeping a tight lid on population growth. This did not quite amount to a "one-child policy", as it is often called (the average number of children per woman was closer to two), but it was highly effective in stabilising numbers. The population will peak at about 1.46 billion in 2030 and then decline gently. Although China has seen stupendous economic growth in recent years, it is still some way off being rich, so it will have trouble absorbing the cost of this rapid ageing. This special report will take a closer look at what it is doing about the problem, but will otherwise confine itself mainly to the developed world.

Fewer hands make heavy work

Macroeconomic theory suggests that the economies of ageing populations are likely to grow more slowly than those of younger ones. As more people retire, and fewer younger ones take their place, the labour force will shrink, so output growth will drop unless productivity increases faster. Since the remaining workers will be older, they may actually be less productive.

In most rich countries the ratio of people of working age to those of retirement age will deteriorate dramatically over the next few decades. In Japan, for instance, which currently has about three workers to every pensioner—already one of the lowest ratios anywhere—the number will halve by 2050. True, there will be fewer young people to maintain, but children cost less than old people and the overall burden will be much heavier than it is now. The OECD has estimated that over the next three decades the age-related decline in the labour force could cut growth in its member countries by a third compared with the previous three decades.

Ageing will affect financial markets too. According to Franco Modigliani's and Richard Brumberg's life-cycle theory of savings, put forward in the early 1950s, people try to smooth out their consumption over the course of their lives, spending more in their youth and old age and saving more in their middle years; so as populations age, savings in the economy as a whole will be run down and assets sold off. This has led to fears of an "asset meltdown" as everyone sells at the same time. But a number of academic studies have so far failed to find much evidence of this. Older people in America, for instance, do save less than those in their middle years, but as a group not much less.

James Poterba, an economics professor at MIT, says America has three kinds of retirement households: the least well-off, perhaps a quarter of the total, who will maintain something close to their previous standard of living on Social Security and Medicare, even with few savings; the richest 10-15%, who hold significant assets and may not need to draw them down; and the large majority in between, who will have to rely on their own, often inadequate, savings in retirement.

For the public finances, an ageing population is a huge headache. In countries where public pensions make up the bulk of retirement income, these will either swallow up a much larger share of the budget or they will have to become a lot less generous, which will meet political resistance (and remember that older people are much more inclined to vote than younger ones). Spending on health, which in most rich countries has been going up relentlessly anyway, is likely to grow even faster as patients get older. And because of a huge increase in the number of over-80s, a lot more money, and careful thought, will be needed to provide long-term care for them as they become frailer.

What can be done? As the IMF puts it, "the fiscal impact of the [financial] crisis reinforces the urgency of entitlement reform." People in rich countries will have to be weaned off the expectation that pensions will become ever more generous and health care ever more all-encompassing. Since they now live so much longer, and mostly in good health, they will have to accept that they must also work for longer and that their pensions will be smaller.

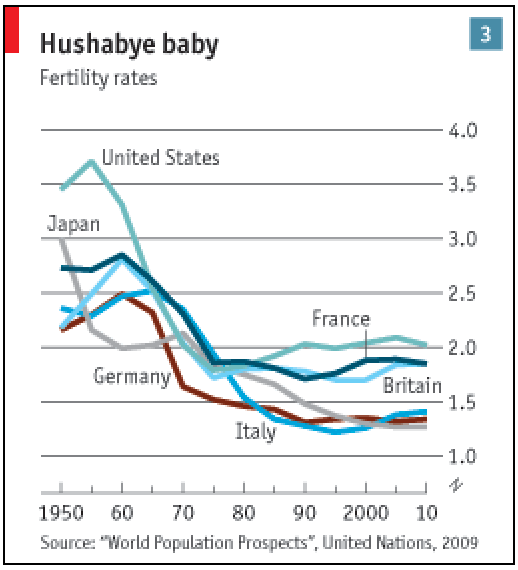
Will the recession make it easier or harder to introduce the required reforms? If people are feeling poorer, they may think that their government should do more for them, not less. Yet some say that if everything is in a state of upheaval already, change becomes easier to bring about. They cite a phrase currently much used in the Obama White House: "Never waste a good crisis."

Suffer the little children

Jun 25th 2009

Most of the rich world is short of babies

IN GERMANY a mother who neglects her children is known as a *Rabenmutter* (raven's mother). Many older Germans slap that label on women with small children who go out to work. Young women in Germany, as elsewhere, are torn. They enjoy their jobs but find it hard to combine them with having a family, for a host of practical reasons such as school hours and lack of child care as well as public disapproval. Faced with that dilemma, some give up work. Others give up having children. About a quarter of the current generation of German women in their 40s have remained childless. The country's fertility rate (the number of children a woman can expect to have in her lifetime) is now a rock-bottom 1.3—the same as in Japan and Italy, where similar attitudes prevail (see chart 3). The chancellor, Angela Merkel, has acknowledged that her country needs to be more child-friendly.



This is not just because children are nice to have. As almost everybody lives ever longer, a reasonable supply of young people is needed to counterbalance—and fund the pensions of—a growing number of older folk. In fact, fertility rates have dropped steeply in all OECD countries in the past few decades, from an average of 3.2 children per woman in 1960 to 1.6 now. The rate needed to keep the population stable (assuming unchanged mortality rates and no net immigration) is 2.1. According to the UN's latest population estimates, fertility is currently below replacement level in over 70 countries, which account for nearly half the world's population. But even in the remaining, poorer, half of the world, fertility rates have come down spectacularly, from 5.2 in 1970-75 to 2.6 now. This has been the most important factor by far in the ageing of populations around the world.

In a few countries where fertility rates are already very low, such as Japan and South Korea, they are still falling. But in others the decline has been arrested and in some, including America, Britain and France, it has been reversed in the past decade or two. That has encouraged governments in a number of rich countries to believe that, with the right policies, they too could boost fertility to closer to replacement levels and help moderate the social burden of ageing. But it will not be easy.

Encouraging women to have more babies used to be politically fraught. Radical feminists everywhere opposed the idea, and in Germany, Italy, Portugal and Spain it carried fascist baggage. But times have changed and now a number of countries are actively encouraging larger families.

Japan has seen especially rapid greying. Immediately after the second world war it was one of the world's youngest developed countries, with a median age of 22. But because so few people were having babies, the median age has doubled since then and is still rising fast. The population, currently about 127m, has already started to decline. It will drop below 100m by 2046 and continue downwards rapidly thereafter, according to a white paper prepared for the Cabinet Office—unless the birth rate can be nudged up (or the Japanese can overcome their dislike of immigration).

A special unit in the Cabinet Office is now working on measures to persuade young Japanese families to do their bit. It is considering things like bigger family allowances, more favourable tax treatment of families and many more nursery places to shorten the long waiting lists. To put more steam behind such initiatives, the government in 2005 appointed a minister for gender equality and social affairs, Kuniko Inoguchi. She has been a tireless campaigner for Japanese women, though her job soon fell victim to a change of government.

Reuters

Just the one, thanks

Will these efforts bear fruit? Florian Coulmas, director of the German Institute for Japanese Studies in Tokyo and author of a book on “Population Decline and Ageing in Japan”, is one of many who think not. He reckons that the only way Japanese women can manage their difficult lives is by postponing marriage and having fewer, if any, children. Because of the country’s culture of long working hours, husbands with good jobs spend little time at home and expect their wives to cope with all domestic tasks. No wonder that 70% of Japanese women stop work when their first child arrives. If they return to it at all it is usually much later, and then mostly to badly paid and unchallenging part-time jobs. By then they may already be caught up in another domestic bind: looking after their husband’s old parents.

Japan is an extreme example, but many other rich countries have similar problems. One reason why there are fewer babies is that women everywhere are marrying and having children much later in life. Between 1970 and 2000 the mean age at which women had their first child in a range of OECD countries rose by more than a year every decade, and many more women now have their families in their 30s. The question is whether they have the same number of children as before but later, or whether they will have fewer overall.

Anna Cristina d’Addio, an expert on fertility policy at the OECD in Paris, thinks they will probably have fewer children in total than if they had started earlier, even though more of them now give birth in their 40s. Surveys show that women generally start off wanting bigger families than they end up with. If the children do not start arriving until later in life, there is less time to reach that ideal number. And once people have got used to smaller families, the number of children they say they want shrinks too. Demographers talk about a “low-fertility trap”.

Postponing marriage and childbirth is part of a bigger change in the lives of many women in rich countries. Over the past few decades many more of them have been getting more highly educated and taking paid jobs. That changed their ideas about what they wanted out of life. For a while birth rates were lower in countries where lots of women worked outside the home, but more recently that trend has been reversed: higher fertility and higher employment rates for women go together.

That may not be as counter-intuitive as it seems. In a modern society children are an economic liability, not an asset. They have to be fed, clothed, housed, looked after, educated and entertained. As a rule of thumb, economists reckon that a family with one child needs 30% more income than a childless couple to maintain the same living standard. The obvious way to keep the household financially afloat is for the mother to go out to work.

If governments anxious to rejuvenate their populations want her to do that, they can help in a number of ways. Extensive research in 16 OECD countries has shown that there is a strong correlation between high female employment rates and large government cash transfers to families, generous replacement pay during parental leave, the availability of plenty of part-time work and lots of formal child care. Where all these things are present, fertility rates tend to go up. France and most of the Nordic countries have embraced such policies and been rewarded with a rise in fertility close to replacement level. It does not come cheap: the OECD reckons that they spend 3-4% of GDP on direct benefits to families, far more than do Germany, Japan and southern Europe.

The odd ones out are America and Britain, which both have lots of women at work and fertility rates close to replacement level (with immigration making up the rest). Neither of them exactly spoils its families with financial inducements or state-provided child care, but their flexible labour markets make it easy for women

to get back into work after childbirth, and public opinion approves of working mothers. They also have high levels of teenage pregnancy that help bump up the figures.

Ms d'Addio says the very low fertility rates now seen in many OECD countries are not inevitable, and governments should try to lessen the obstacles to childbearing faced by individuals and families. But having children is a personal choice, and if people really do not want them there is nothing governments can do. The UN expects fertility in developed countries to recover somewhat by 2050, to 1.8 children per woman, but many experts think that forecast is too optimistic.

A world of Methuselahs

Jun 25th 2009

The benefits, and the costs, of living longer

IT IS written in the Bible's Book of Genesis that Methuselah lived to be 969. He held the record, but there seem to have been plenty of other multicentenarians around at the time, including Noah and old Adam himself. Their ages are not to be taken literally. In another part of Genesis, man's lifespan is put at a mere 120 years. The person with the longest documented life in modern times, Jeanne Calment, reached 122, but no one else has come close.

In most of recorded history even the more familiar three score years and ten was rare. Angus Maddison, an economic historian, has estimated that life expectancy during the first millennium AD averaged about 25 years (which in practice meant that lots of children died very young and many of the rest survived to middle age). The big turnaround came with the industrial revolution, mainly because many more children survived into adulthood, thanks to better sanitation, more control over epidemics, improved nutrition and higher living standards.

By the beginning of the 20th century average life expectancy in America and the better-off parts of Europe was close to 50, and kept on rising. By mid-century the gains from lower child mortality had mainly run their course. The extra years were coming from higher survival rates among older people. The UN thinks that life expectancy at birth worldwide will go up from 68 years at present to 76 by 2050 and in rich countries from 77 to 83. (These are averages for both sexes; women generally live five or six years longer than men, for reasons yet to be fathomed). Most experts now agree that there will be further rises, but disagree about their extent.

Things fall apart

Some of them argue that the human lifespan is finite because bodies, in effect, wear out; that most of the easy gains have been made; and that the rate of increase is bound to slow down because people now die mostly of chronic diseases—cancer, heart problems, diabetes—which are harder to fix. They also point to newer health threats, such as HIV/AIDS, SARS, bird flu and swine flu, as well as rising obesity in rich countries—to say nothing of the possibility of fresh pandemics, social and political unrest and natural disasters.

Nearly 30 years ago James Fries at Stanford University School of Medicine put a ceiling of 85 years on the average potential human life span. More recently a team led by Jay Olshansky at the University of Illinois at Chicago said it would remain stuck there unless the ageing process itself can be brought under control. Because infant mortality in rich countries is already low, they argued, further increases in overall life expectancy will require much larger reductions in mortality at older ages. In Mr Olshansky's view, none of the life-prolonging techniques available today—be they lifestyle changes, medication, surgery or genetic engineering—will cut older people's mortality by enough to replicate the gains in life expectancy achieved in the 20th century.

Panos

That may sound reasonable, but the evidence points the other way. Jim Oeppen at Cambridge University and James Vaupel at the Max Planck Institute for Demographic Research in Rostock have charted life expectancy since 1840, joining up the figures for whatever country was holding the longevity record at the time, and found that the resulting trend line has been moving relentlessly upward by about three months a year. They think that by 2050 average life expectancy in the best-performing country could easily reach the mid-90s.

Rises in life expectancy have been habitually underestimated because it seemed unlikely that the improvement could go on for ever, and just as regularly the figures have had to be revised soon afterwards. Some

experts now think there may be no theoretical limit at all, pointing to the huge rise in the number of centenarians in the past few decades. In America they are the fastest-growing section of the population, with an increase from 3,700 in 1940 to over 100,000 now.

Blessing or curse?

Why are people living ever longer? Robert Fogel at the University of Chicago, a Nobel prize-winner in economics, reckons that improved medical care and technology are only part of the answer. Another part, he thinks, is something he has dubbed “technophysio evolution”. Over the past few centuries humans have developed more resilient physiques because they gained unprecedented control over their environment and their living conditions. Western people’s average body size has increased by 50% over the past 250 years. Larger body size (but not obesity), Mr Fogel’s research has shown, is associated with better health and longer life.

But modern life has its downsides too. Stress is often seen as a life-shortening factor—though perhaps the effects are not as lethal as some people think, or else the Japanese, who are famous for working long hours, would not have the highest life expectancy in the world.

Another hazard of affluence is getting fat. Around 10-20% of the adult population in many rich countries, and over 30% in America, are now clinically obese. Overweight people are at greater risk of cardiovascular and respiratory diseases, cancer, type-II diabetes and other life-shortening ailments—though it is not yet clear whether the effects are strong enough to cancel the trend to greater longevity.

And life expectancy can go down as well as up. In much of eastern Europe it started dropping in the 1980s in response to the upheaval in the region, and despite a subsequent slight recovery it has still not regained the level of the 1960s.

People almost everywhere could extend their life spans further just by doing a few sensible things, such as not smoking, drinking only in moderation, eating lots of fruit and vegetables and taking regular exercise. Educated folk are better at keeping to such rules, and as a group they live markedly longer than those with only basic schooling. Richer people, unfairly, also live longer than less well-off ones, even in the developed world.

But all this is tinkering at the edges. Mankind’s dream has been to conquer ageing altogether, and scientists are working on it. Spare-part surgery to replace worn-out bits of the anatomy is already well-established and will get better with the use of stem-cell technology. For a more general effect, experiments on rodents have shown that a severely restricted but balanced diet can increase their lifespan by about 30%. But nobody knows whether this would work in humans, and even if it did, there might be few takers.

The longer-term hope is to find a way of switching off the ageing process by manipulating the appropriate genes, which in theory could make people near-immortal (though they could still die of accidents and diseases). But if that were feasible, the consequences would need to be carefully thought through. In Jonathan Swift’s “Gulliver’s Travels”, the hero meets a tribe of immortals, the Struldbruggs, who far from being wise and serene turn out to be a miserable lot: “Whenever they see a funeral, they lament and repine that others have gone to a harbour of rest to which they themselves never can hope to arrive.”

Hale and hearty

People in the rich world can now expect to live, on average, more than a quarter of a century longer than they did 100 years ago. Is that a blessing or a Struldbruggian curse? Clearly it depends on whether they become old and frail at the same age as before and just limp on for much longer, or if the extra years are hale and hearty ones.

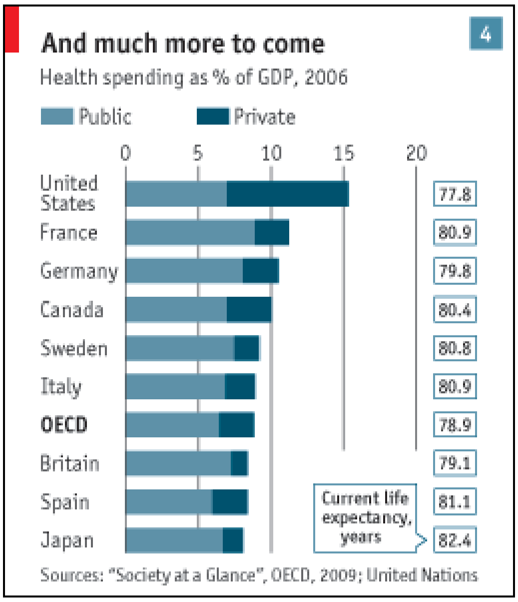
Most of the evidence supports the more cheerful view. Research led by Kenneth Manton at Duke University found that in recent years disability above the age of 65 in America has been falling significantly. In other rich countries the picture is more mixed. When the OECD recently looked at 12 member countries, it found clear signs of a recent decline in disability in elderly people in only five of them (including America). But other studies produced more optimistic results.

By and large, people do now seem to remain in good shape for longer. Moreover, the period of ill health that usually precedes the final goodbye has got shorter in the past few decades, which demographers call "compression of morbidity" (as a rule of thumb, the bulk of spending on an individual's health care is concentrated in the last year or two of life, and particularly in the final six months). This compression has a variety of causes, including the shift from manual to physically less demanding white-collar work, rising levels of education and much-improved health care and medical technology, from keyhole surgery to heart pacemakers. Eighty, it is said, is the new 65.

But even fairly fit older people need more health care than younger ones, not least because they often suffer from chronic diseases that are expensive to treat. In the EU, one estimate puts health-care spending on the elderly at about 30-40% of total health spending. So will the better health of an ageing population, good as it has been for so many, impose unaffordable costs on public-health budgets?

Over the past few decades all OECD countries have seen their health spending grow considerably faster than their economies. Ageing populations will add further momentum to that growth. Howard Oxley, a health-care expert at the OECD, reckons that increased spending on health and long-term care for the elderly could amount to an extra three-and-a-half percentage points of rich countries' GDP by the middle of the century—and a lot more if spending on medical technology continues to go up at current rates.

Measured by spending on health care as a share of GDP, America already tops the list, shelling out the equivalent of more than 15% of GDP (see chart 4). The American government's health-care spending will be hugely affected by ageing because of Medicare, the state-funded health-care programme for the elderly and disabled, and Medicaid, the programme for the poor (and often also old, because it covers long-term care).



President Barack Obama is determined to reform his country's health-care system to improve coverage and, eventually, drive down costs. More money does not always produce better results. People in America are less healthy and die sooner than in Britain, which proportionately spends little more than half as much on its health care. According to David Cutler, an economics professor at Harvard who has advised the president on the reform, even doctors believe that around 30% of money spent on health care in America is wasted.

Peter Orszag, head of the Office of Management and Budget, has recently been praising the work of a group of medical experts at Dartmouth Medical School, led by Elliott Fisher, which has been compiling an atlas of regional variations in American medical practice and health-care spending, mainly for people on the Medicare programme. It found that in 2006 Medicare spending varied more than threefold across American hospital referral regions. Again, higher spending does not seem to result in better care or greater patient satisfaction. Because the system has encouraged the provision of lots of doctors, specialists, hospitals and expensive diagnostic kit, all of them are kept busy without much regard to results.

The trouble with health care in America, says Muriel Gillick, a geriatrics expert at Harvard Medical School, is that people want to believe that "there is always a fix." She argues that the way Medicare is organised encourages too many interventions towards the end of life that may extend the patient's lifespan only slightly, if at all, and can cause unnecessary suffering. It would often be better, she thinks, not to try so hard to eke out a few more hours or weeks but to concentrate on quality of life.

Take care

But long before they get to that point, growing numbers of old people will become less able to look after themselves and need more care. Across the OECD, spending on long-term care is already equivalent to around 15% of total health spending and is rising fast. The great bulk of that care—an estimated 80%—is still provided by family and friends, the traditional source of support for the elderly. But more women are going out to work, so fewer of them have time to look after old folk and formal help is becoming increasingly important.

In most developed countries only a small minority of over-65s—between 3% and 6%—live in institutions. Keeping old people in nursing homes or hospitals is expensive, staff is hard to find, and in any case most people would much rather be looked after at home. Many countries are now providing grants to adapt homes, paying families for the care they provide and supplying helpers to give a hand with things like dressing and bathing.

With far more people reaching a great age, a lot more such care will be needed in future. How will it be paid for? A few far-sighted countries—including Germany, the Netherlands, Luxembourg and Japan—have already introduced mandatory long-term-care insurance schemes. Others may have to follow.

The silver dollar

Jun 25th 2009

There is money to be made in the grey market, but it takes thought

WHEN Tokyo residents of a certain age want to go shopping, they head for Sugamo, in the north of the city. The main street, Jizo-dori, features a variety of shops selling food, sweets, medicaments, bits and bobs and, most notably, a huge choice of woolly underwear in bright red, a favourite colour with the elderly because it is thought to be lucky and health-giving. The local McDonald's has a section with seats designed for older people, and a karaoke bar offers songs from the good old days. For spiritual refreshment, there is the four-centuries-old Kogan-ji Buddhist temple, where visitors buy incense and pray for a long life—and a quick and easy exit.

Jizo-dori has a long tradition, but businesses everywhere now realise that in future there will be a lot more older folk with money to spend. In most rich countries the baby-boomers born after the second world war were more numerous, better educated and better paid than any generation before them. When those boomers retire, they will want to do it in style, plastic surgery and all.

What else might they spend their money on? The glossy magazine published by America's AARP, a powerful lobbying organisation for the over-50s that boasts 40m members, is bursting with ads. If those advertisers have got their market right—and they are paying big money for the older eyeballs—this group of customers can be persuaded to buy a plethora of products, from travel and financial services to mobile phones, medicines and comfy beds.

Some businesses are already adjusting their ranges to cater for the grey market. Volkswagen, for example, has developed a car called the Golf Plus that has higher seats and more space than the standard model. A number of consumer-goods makers have started making smaller pack sizes for older, smaller households.

Alamy

Jizo-dori's temptations

Japan, which has already had lots of practice with older consumers, has developed some ingenious new products for the grandparent generation. They include a furry robot seal, sold as a pet substitute, that has proved a hit with lonely old folk. And makers of personal-care products recently put on a Tokyo fashion show for incontinence pads, featuring pink and frilly varieties instead of the dull old white sort.

This is a tricky market to tackle. Advertisers are often accused of trying too hard to sell to the young when much of the spending power is now concentrated in older age groups, but it is not a simple matter of moving "from rocking horse to rocking chair". When companies try to cater for older customers, they do not always get it right. Attempts to "seniorise" ads, for example, have mostly drawn a poor response because their targets think of themselves as younger than they really are. That refusal to settle for being "old" will only get stronger as the baby-boomers start turning 65.

But the hardest thing about selling to older people is that they are such a heterogeneous group. Someone in his 70s may be in frail health and living in an old folks' home; or he may be running for president of the United States, as John McCain did last year. There are many shades of grey.

Scrimp and save

Jun 25th 2009

Pensions will have to become far less generous

THE past few decades have been the cushiest time ever to be a pensioner in a developed country. Not only has the world been getting ever richer (at least until very recently), which rubbed off on pensioners too; but as a group they have also become much more comfortable relative to the rest of the population. In recent years mandatory pensions across the OECD, net of taxes and social-security contributions, averaged over 70% of previous net earnings for people on average pay and over 80% for the low-paid. For the better-off the replacement ratio was lower, but they can cope.

The official retirement age in most countries has stayed much the same even though people are living a lot longer, so pensioners have been getting more years in which to enjoy themselves without the pressures of work. In fact, many of them stopped working well before it was time for their gold watch because they were offered irresistible inducements to go early. In Austria, for instance, the official retirement age for men is 65 but the average actual age is 59, which means that many of them leave even earlier.

Being generous to pensioners was affordable in 1980, when in the rich world there were only about 20 people of retirement age for every 100 people of working age. But that ratio has already risen to 25% and by 2050 it will be around 45%, meaning that there will be only about two workers for every pensioner. In some countries things will be much worse: Japan is heading for a ratio of over 70%. Something has to be done.

The most urgent need for reform will be in public pensions, which in most developed countries are the biggest source of retirement income. They usually make up most if not all of the pensions of low and medium earners. Most of these pensions work on the pay-as-you-go (PAYG) principle, whereby today's workers pay for today's pensioners, on the understanding that the next generation will do the same for them when their time comes.

Now that labour forces are starting to contract and the number of pensioners is rising, these schemes are rapidly becoming unsustainable. One theoretical answer is to move to funded schemes, in which pensions are paid out of a big pot of accumulated savings. Such schemes are common in the private sector, but a public PAYG scheme is very hard to turn into a funded one because one generation of workers would have to pay both for themselves and their parents' generation.

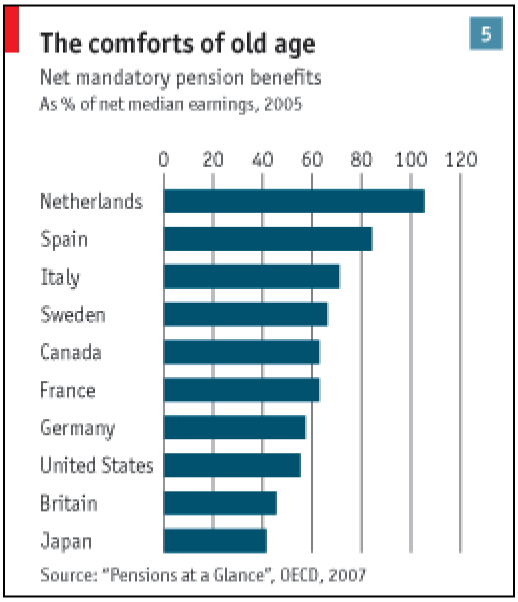
Unsustainable

Many rich countries already spend around 8% of GDP on public pensions, and some—Germany, Italy, France—a lot more. Richard Jackson at the Centre for Strategic and International Studies (CSIS), a think-tank in Washington, DC, calculates that if nothing is done the cost of state pensions in developed countries will almost double, from an average of 7.7% of GDP now to about 15% by 2050. In Japan and some "old" western European countries it could rise to well above 20%.

In a "no-change" scenario public expenditure on health would also rise steeply, so by 2050 the developed world would be spending nearly a quarter of its GDP on these two items alone. To prevent increases on that scale, about half the rich countries have already introduced various reforms over the past decade that have made their pensions less generous. Many more cutbacks are bound to follow.

The most obvious thing that needed reconsidering was the retirement age. When America introduced its Social Security (public pension) scheme in 1935 to prevent poverty in old age, the retirement age was 65 and life expectancy at birth was 62. In 1983

a decision was made to raise the official retirement age to 67, but in steps so tiny that the move will not be completed until 2027. Life expectancy at birth in America now averages about 78, so the promise of a pension is worth a great deal more than it was back in the 1930s. As it happens, America's public pension system is among the rich world's less generous (which means that financing it should remain manageable), but it still accounts for more than half the average pensioner's income.



In the past few decades a number of governments offered various carrots to encourage people to start drawing their pensions before the official retirement age. They often claimed that this would free up jobs for younger people. Any economist could have told them that this was a prime example of the "lump-of-labour" fallacy (the idea that there is only a fixed number of jobs in an economy at any one time) and would not work. It didn't, but the workers were happy to go and their employers were happy to lose them. Private defined-benefit final-salary schemes (explained below), where they existed, also encouraged early retirement because they did not impose an actuarial penalty on people leaving before the due date.

All this meant that the actual ("effective") retirement age in many rich countries, particularly in Europe, dropped well below the official one. By 2004 in the OECD as a whole only 60% of people aged between 50 and 64 were working (compared with 76% for those aged 24 to 49). It was the opposite of what was needed to deal with rising life expectancy, so in recent years governments in many countries have started to dismantle some of the incentives to leave early, against fierce political resistance. This has halted, and in some cases reversed, the trend towards ever earlier retirement.

But that is only a beginning. Italy, which had a particularly unaffordable public pension scheme, has not only raised the retirement age but also increased the number of contribution years needed to qualify for a pension and cut back on benefits for the highest earners—though the effects will be felt only by people who retire from 2017 onwards. A number of other countries are gradually reducing the replacement rate of their pensions, particularly for the better-off, though most of them have been careful not to squeeze the poorest pensioners too hard.

Good try, but it didn't work

Reuters

There goes my 401(k) plan

Britain, unusually, found itself having to move the other way. Its state pension had become impossible to live on, thanks to a little-noticed decision by a Conservative government in 1980 to link the rise in the state pension to living costs instead of average earnings. In 2006 a government-appointed commission chaired by Lord Turner recommended reinstating the link with earnings, which is due to happen in 2012. Britain's solution to the problem of unaffordable public pensions—to downsize them and hope that the private sector would fill the gap—had proved untenable.

Now the debate about sustainable pension systems for the future is all about spreading the load over several pillars. There should be a basic state pension to meet basic needs in old age, perhaps with an earnings-related element on top of it; a private occupational pillar, with employers and employees both making contributions; and a voluntary pillar, with private individuals saving for their retirement through a variety of instruments. Governments are expected to do their bit not only by providing the state-funded part, but also by offering tax incentives for the second and third pillars.

To take the pressure off public pensions, many governments have encouraged private pension plans, which have expanded rapidly in the past ten years. In half the members of the OECD private pensions are now either mandatory or cover the vast majority of the workforce. In some countries, including America, Australia, Denmark and Switzerland, private pensions now account for

up to half of total retirement income.

But even before the recent financial crisis it was clear that shifting more responsibility for retirement income to the workers themselves raises big problems. In countries where public pensions are relatively small, such as America, Britain and Ireland, people are simply not saving enough to maintain their living standards in retirement. McKinsey, a consultancy, recently looked at the finances of a large sample of baby-boomers, due to start drawing their pensions soon, and found that about two-thirds of them had failed to make enough financial provision for their retirement to maintain their previous standard of living, even though as a group they had always earned well. That fits with the trend of a steady decline in American personal saving rates in the past 20 years.

And even those who had been putting money by for their old age may now be having second thoughts. In America one of the main vehicles for occupational pensions are 401(k) plans, named after a section in the Internal Revenue Code that allows employees to make tax-free payments into a defined-contribution plan. Employees can choose from various investment options, usually a range of mutual funds. Last year's stockmarket crash caused a huge drop in the value of most such plans. Many people who had planned to retire in the near future found they had to carry on working. Suddenly prudence did not seem such a good idea.

In countries where private occupational pensions play a large part, such as America and Britain, they have become less opulent and more uncertain. In recent years there has been a big shift from defined-benefit schemes (where the eventual pension depends on a formula that takes into account the level of pay and years of contributions) to defined-contribution schemes (where a certain level of contribution is agreed on and the money invested, with the eventual pay-out depending on the return on that investment).

Defined-benefit schemes worked fine as long as stockmarkets were rising, enabling companies with such schemes to take "pension holidays"—putting a freeze on further contributions because their investments had done so well. But when markets turned down, large holes opened up in companies' pension funds that had to be filled from current operations. Life expectancy also proved longer than forecast.

Defined-contribution schemes avoid such problems for the companies by handing all the risks to employees. It is the employees who have to worry about how their pension investments will perform and whether they will have enough to live on when they retire. If their pension funds are invested in their own company (not recommended, but it happens), they could lose everything, as workers at Enron, an energy company that collapsed spectacularly in 2001, found to their cost. Most people do not know enough about finance to make informed investment decisions.

In America, which began to move away from defined-benefit schemes two decades ago, defined-contribution plans already account for the great majority of private-sector pension schemes. Companies in Britain started later but advanced faster. Earlier this month two large British companies, BP and Barclays, announced they were closing their defined-benefit schemes, respectively, to new and existing members. Defined-contribution plans are not only riskier for the employee, but companies often contribute less to them and the resulting payouts are smaller.

In future, a growing number of people will have to manage on less generous and more uncertain occupational pensions. The big exception are public-sector workers, typically accounting for 10-20% of the total workforce in rich countries, who for the most part continue to enjoy good defined-benefit pensions. But their privileges are now coming under fire.

So if state pensions are having to be reined back, private pensions are getting meaner, riskier and less predictable, and money saved for retirement is threatened by financial crises, what is the man in the street to do to make ends meet? The only thing for it, say all the experts in unison, is to carry on working.

Work till you drop

Jun 25th 2009

Retirement has got out of hand

HOW much golden leisure can you expect at the end of your working life? The OECD has calculated for how many years people in its member countries are now likely to be drawing their pensions, starting not from their official but their actual retirement age. It found that men could look forward to between 14 and 24 years in retirement and women between 21 and 28 (see chart 6). In many countries that was half as long again as in 1970, and in some of them twice as long. And the figures are probably an underestimate because they are based on life expectancy as it is now, not as it will be in future.

Retirement has been overdone. The original idea was that people should enjoy a bit of a rest after a life at work, but nobody imagined that the rest would stretch to almost a quarter-century. Some countries have already raised their official retirement age; others are debating whether it still makes sense to have a specific retirement age at all. One widely touted idea is to phase in retirement over a number of years. It does not seem like a good idea for people to be working at full tilt one day and twiddling their thumbs the next.

From an economic point of view, getting people to work for a few more years would solve many of the problems associated with ageing populations. By carrying on, those workers will not only save the public purse money by not drawing a pension but will also continue to pay taxes and social-security contributions, so those extra years are doubly valuable.

Moreover—though it seems an outlandish thought in the middle of a deep recession and rising unemployment—ageing populations are likely to cause labour shortages. In some countries and some sectors these are showing up already. In Germany, where the labour force is due to start shrinking from next year, a study by the Institute for the German Economy in Cologne identified a shortage of about 70,000 engineers in 2007, a rise of nearly half on the year before. The obvious place to look to fill such gaps is among well-qualified older people, and indeed the institute found that companies had stepped up their recruitment of engineers over 50.

Many countries already have laws to prevent discrimination on age grounds. America led the way with its Age Discrimination in Employment act in 1967, designed to make sure that the over-40s (greybeards of their day) were given the same job chances as younger people. Among other things, it prohibited reference to age in job advertisements. The act has since been amended a couple of times and now rules out mandatory retirement on age grounds for most jobs. That seems to have helped keep older workers in jobs.

The European Union in 2000 issued a directive that obliges member countries to ban discrimination in employment on a number of grounds, including age. France imposes a tax called the Delalande contribution (now being phased out) on employers who sack older workers. Although this can be quite hefty—up to a year's pay—it does not appear to have saved many jobs. Rather, it has discouraged employers from hiring older workers.

Various countries have concocted an alphabet soup of initiatives and pilot projects to get older people into work and keep them there, with mixed results. Advocacy groups for older people such as America's powerful AARP, and a growing number of similar organisations that are springing up in other rich countries, have helped to raise awareness of the issue. But survey after survey finds that where employers have a choice, they prefer to hire younger workers. Are they right?

On the face of it, there are plenty of reasons to plump for youth. In most countries, pay goes up as workers

become more experienced and productive, and then declines again towards the end of their careers. But in some places—for example, France, Germany and Spain—pay just keeps rising. So even assuming that workers remain just as effective as they get older (see below), at some point they end up being too expensive for what they offer.

But employers are also doubtful that older workers can still hack it. Vegard Skirbekk of the International Institute for Applied Systems Analysis near Vienna has reviewed a large number of studies about the relationship between age and individual productivity and found a fairly broad consensus that productivity in many jobs declines substantially in mid-working life.

Panos

It all depends what you mean by work

Now that so-called "3D jobs"—the dirty, dangerous and demanding sort in, say, mining or steelmaking—have become thinner on the ground, it may not matter so much if workers become physically less vigorous; besides, older people are in better general health these days. But there is plenty of evidence that by the time people are 50, some of their cognitive abilities have also started to decline. In particular, a quality called "fluid intelligence"—including numerical skills and the ability to adjust rapidly to new situations—begins to go downhill in middle age. Very brainy people generally do their most innovative work before they are 40. Nobel prizes are usually awarded for achievements fairly early in life. By contrast, "crystallised intelligence"—general knowledge, experience, verbal ability—continues at much the same level almost indefinitely.

Employers think that older people may find it harder to pick up new skills, particularly in IT, which have become indispensable for many jobs. But that may be partly because they are invariably offered less training than younger ones. The argument is that they will be leaving soon and are not worth investing in. But younger employees might leave too.

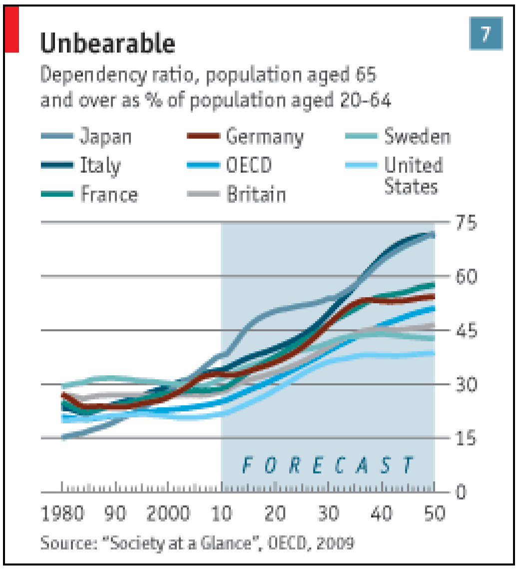
All these reservations are linked to older workers' individual capabilities. But Axel Boersch-Supan at the Mannheim Research Institute for the Economics of Ageing and his team have argued that what matters in a modern economy is the productivity of teams of workers, not individuals. The best solution may be to employ a mixture of vigorous young and experienced older workers.

Older workers' knowledge and experience can easily be lost to the company when they retire. In a recent article in the *Harvard Business Review* based on his work with RWE, a German energy company, Rainer Strack of the Boston Consulting Group advises managers to conduct an audit of how the ageing of their workforce will affect them in years to come and develop a strategy to make sure they maintain the right skills mix.

Show me the colour of your carrot

But even if employers were happy to keep or recruit older workers, how enthusiastic would those workers be to carry on? That would depend on the circumstances. In the past few decades, when pensions in most rich countries were reasonably generous and early retirement was positively encouraged, only the most workaholic (or improvident) continued working. But now that money is getting tighter and early-retirement deals are off, the balance may well have shifted.

Most of America's baby-boomers now say that retirement is not for them, partly because they fear they may not be able to afford it and partly because they actually like work. In Europe too there has been a change of heart from the retirement-minded 1980s and 1990s. In a recent FT/Harris poll 45-60% of respondents in the big European countries favoured working longer for a bigger pension (except in Germany, where only about a quarter wanted to carry on). But many older people would like a less onerous workload than they had at their peak, perhaps working part-time.



Japan, where it is customary to work well beyond the official retirement age, has found ways to allow people to step into less demanding roles. For example, at the head office in Tokyo of Hitachi, a giant global electronics company, over two-thirds of those who reach the company retirement age of 60 apply to be rehired. The company can usually find jobs for them, explains Takane Miwa from the company's human-resources department, but often in a different division, sometimes part-time and always minus their former job title and seniority. The company pays the employee about 80% of his previous salary, which includes his public pension and a government subsidy, so it gets him at a bargain price.

Most other rich countries have not been good at making use of older people willing and able to work. The names of a few companies that have consistently recruited staff past retirement age—mostly retailers such as Britain's B&Q and America's Wal-Mart—pop up time and again, but the list never seems to get much longer. In the absence of a good choice of jobs, some newly retired people manufacture their own, turning themselves into self-employed consultants to do much the same thing as before, though perhaps at a less punishing pace.

It is worth bearing in mind that if many more older people were to stay on in the formal economy, some of the things they now do outside it and without monetary reward would fall by the wayside. Many newly retired folk sign up for voluntary work, and many more get drafted into family duties, looking after grandchildren or frail old parents. Such unpaid work does not show up in the GDP figures. If the people who do it held down regular jobs, much of those things would have to be paid for—or would not get done at all.

China's predicament

Jun 25th 2009

Getting old before getting rich

THE Beijing Ren Ai Geracomium is set in a drab, dusty village just outside the Chinese capital. Grouped round a pleasant garden, this old people's home for about 80 residents, aged from 50 to 96, is unusual in several respects. Its private owner is a Christian, and the home has a small chapel where the handful of Christian residents, along with other people of that faith living in the area, gather for Sunday services. The home is run as a commercial enterprise, but Hu Wenru, its deputy director, says that since it opened three years ago it has been only gradually building up business and is not yet making a profit. Still, the owner is already preparing to launch a second one with 300 beds in the next village, so he must be confident of success.

The main thing that makes Ren Ai unusual is that it exists at all. Old people's homes are a rarity in China, catering for only about 1% of the over-65s, far less than in most Western countries. The vast majority of older Chinese live with their families. Care for the old within the family is not only a cultural expectation, based on the Confucian tradition of respect for age and experience; under a law passed in 1996 it is also a legal obligation. Elderly people have been known to sue their families for maintenance if they fail to comply.

At present, institutional care is the last resort for those who have no family or who need so much help that their relatives cannot cope. Many of the residents at Ren Ai, for example, have serious physical or mental problems, and the home has two full-time doctors on the staff. The place is clean and seems well-run, but it is spartan: some of the rooms sleep six people, with one basic bathroom between them. Even so, the fees are much higher than most ordinary people can afford, averaging 1,300 yuan ($190) a month for the reasonably fit but with extra charges for those who want a single room or need lots of nursing. Some of the residents are subsidised by the government, which seems happy to let private initiative flourish.

Panos

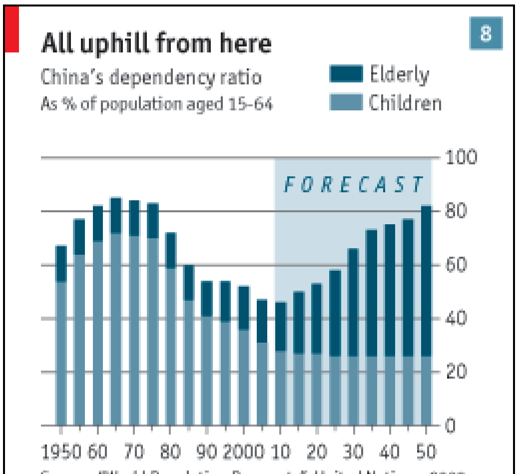
Plenty of life after work

There will be a lot more need for institutional care for elderly people in future, says Du Peng, director of the Institute of Gerontology at Beijing's Renmin University. For the past three decades China has been operating a strict population-control policy, so there are now far fewer young people around to take care of the elderly. This state of affairs is usually referred to by the nifty formula "4-2-1", meaning that the typical only child today will have two parents and four grandparents to look after—a bit of an exaggeration, but not that far off.

It has also become harder for families to live together because people move around a lot more than they used to. An estimated 150m migrant workers have left their rural homes for jobs in the big cities, though many of them might return home eventually. Most importantly, because of the low birth rate and rising life expectancy, the number of over-60s is expected to go up very rapidly, from about 166m now to 342m in only 20 years' time. All this means, says Mr Du, that many more older folk will be living in institutions.

China is still a relatively young country, with a median age of around 30. But, uniquely among developing countries, it is ageing extraordinarily fast, so by 2050 its median age will have risen to about 45. Over the next few decades the ratio of elderly dependants to people of working age will rise steeply, from 10% now to 40% by 2050. From about 2030 the country will have more elderly dependants than children (see chart 8), whereas in most other developing countries the opposite will remain true for the next few decades. China's pattern of ageing is very similar to that in Japan, Hong Kong, Singapore, South Korea and Taiwan. The difference is that in China this is happening at a time when the country is still relatively poor.

The man who lays claim to having invented the phrase "getting old before getting rich", in the early 1980s, is Wu Cangping, an academic at the Population and Development Research Centre at Renmin University. At that time population ageing was receiving little attention, and he wanted to shock the government into preparing for it. Since then China has become a lot richer (with an income per person of about $6,000 at PPP)—though not nearly as rich as most developed countries when they were starting to age. Some Chinese demographers are now arguing that the phrase should be amended to "getting old while getting rich".



Source: "World Population Prospects", United Nations, 2009

In search of a new rice bowl

Whether poor, rich or somewhere in-between, China will certainly need to spend some money to provide a basic social safety net for its people, not just the old but everyone. Until about 20 years ago the vast majority of urban workers were covered by a system known as the "iron rice bowl". People who worked for the state, in state-owned companies or in state-approved collectives, enjoyed cradle-to-grave benefits ranging from housing, education and health care to a generous pension scheme, with an official retirement age of 55 for men and 50 for women for manual workers (but five years more for white-collar workers) and a replacement rate of about 80% of final salary. Most people retired about five years before the official age.

It was too good to last, and it didn't. In the early 1990s huge number of state-owned enterprises were shut down and jobs in those that survived were savagely cut. Many state firms passed into private hands and new private companies grew up alongside them. Whereas civil servants and employees in state-owned firms used to make up nearly 80% of all urban workers, their share is now down to 20%. The government is committed to honouring the pension promises left over from the old system, but the iron rice bowl has gone. That has left a huge gap in urban workers' social-security provision. Workers in rural areas, who still make up about half the total labour force, never had much coverage of any kind anyway.

Since then the government has launched a series of initiatives to put a new welfare system in place. The main concerns are health care and pensions. Since the demise of the old system, health-insurance coverage has been patchy and in rural areas mostly non-existent. Health insurance is generally not portable, so if people move from one part of the country to another they may lose their coverage. But even if covered, people have to make large co-payments, which for the elderly and those with serious health problems can be crippling. A survey carried out in 2000 by the China Research Centre on Ageing, a think-tank, found that more than half the over-60s' medical expenses came out of their own pockets and a big chunk of the rest was paid for by their families.

In April the government set out its plan for a comprehensive reform to build a "safe, effective, convenient and affordable" health-care system by 2020. Over the next three years it intends to spend 850 billion yuan. By 2011 more than 90% of the population is meant to be covered by the system. In rural areas that figure has already been reached, but the scheme usually covers only in-patient treatment and the reimbursement rate remains very low.

The pensions system too is in flux. In the early 1990s the government announced a three-pillar scheme along the lines of those in many developed countries: a basic pay-as-you go pension to which both employers and employees make mandatory contributions; funded individual accounts, also with contributions from employers and workers; and individuals' private savings. This is a work in progress. Reforms are being announced "almost annually", says Wang Yanzhong, who heads the Centre of Labour and Social Security Studies at the Chinese Academy of Social Sciences (CASS).

So far only about a third of the population is covered by any kind of pension scheme. The funded individual accounts envisaged under the government's plans have been set up, but so far there is little money in them. Because of restrictions on investment abroad and a dearth of high-yielding instruments at home, such money as has accumulated has been invested mainly in the domestic banking system, where it earns a rate of return far too low to meet the government's pension promises.

Jonathan Anderson, a China specialist at UBS, calculates that under the current pension system the government could face unfunded liabilities of up to 6% of GDP annually a few decades hence. But it could head them off by a variety of means: raising contributions or increasing coverage to bring more money into the system; increasing the retirement age; securing better returns on the accumulated funds; or reducing future pay-outs.

By far the most effective way, though, would be to raise the retirement age. In early spring the government hinted that it was considering such a move, but Chen Chuanshu, vice-director of the government's high-powered National Committee on Ageing, says there are "diverse views" on the matter. In principle it seems a good idea. Average life expectancy at birth, at 74, is now 25 years higher than it was 50 years ago, yet the retirement age has remained at the same low level. Unless it goes up, any comprehensive pension system that China might eventually introduce will be hideously expensive.

In practice, though, both workers and employers are strongly opposed to a change. Workers have got used to the idea of retiring in their 50s and planned their lives accordingly. Employers have had the luxury of being able to pick from a seemingly inexhaustible supply of vigorous people in their 20s and 30s. Workers in their 40s are already considered old, and many of those in their 50s may indeed lack the skills needed in a modern economy.

But given the low birth rate over the past 30 years, the supply of young workers is not, in fact, endless. Cai Fang, director of the Institute of Population and Labour Economics at CASS, points out that there is already a shortage of young migrant workers; it started in the coastal areas in 2004 and has now spread everywhere. The worldwide economic downturn has temporarily eased the pressure, but employers in China's coastal boom belt continue to complain of shortages (although 20m people are said to have lost their jobs since the downturn hit late last year).

So there is now an economic, as well as a human-rights, case for relaxing the country's "one-child policy". Many Chinese academics think it can be only a matter of a few years, but the government seems in no hurry. "Family planning", as it likes to call the policy, is seen as a success, easing pressures on the environment and resources of all kinds. There is no explicit population target, but the latest forecasts suggest that numbers will keep growing from about 1.3 billion now to a peak of around 1.46 billion by 2030 and then start declining gently.

In fact, even if the restrictions were loosened immediately the birth rate might not tick up by very much. In the big cities many people are already leading the sort of lives that have brought down fertility in richer countries.

China's government is well aware of the problems of an ageing population, and "is doing all the right things but not always fast enough", says Vanessa Wang, an Asia specialist and actuary with Mercer, a consultancy. So far the government's main priority has been to keep up the prodigious economic growth rates of recent years, but the prime minister, Wen Jiabao, has said that the government is attaching growing importance to social welfare.

Of the 4 trillion yuan economic-stimulus package announced last November, 300 billion has now been reallocated from infrastructure projects to welfare schemes. Critics say China could afford to do much better. Its public finances are in good shape, with its public debt at less than 20% of GDP and its fiscal balance improving rapidly. Saving, at over 40% of GDP, is high by international standards. Given the prospect of 440m pensioners by 2050, perhaps it should invest more in creating its much-advertised "harmonious society".

Into the unknown

Jun 25th 2009

The world has never seen population ageing before. Can it cope?

UNTIL the early 1990s nobody much thought about whole populations getting older. The UN had the foresight to convene a “world assembly on ageing” back in 1982, but that came and went. By 1994 the World Bank had noticed that something big was happening. In a report entitled “Averting the Old Age Crisis”, it argued that pension arrangements in most countries were unsustainable.

For the next ten years a succession of books, mainly by Americans, sounded the alarm. They had titles like “Young v Old”, “Gray Dawn” and “The Coming Generational Storm”, and their message was stark: health-care systems were heading for the rocks, pensioners were taking young people to the cleaners, and soon there would be intergenerational warfare.

Since then the debate has become less emotional, not least because a lot more is known about the subject. Books, conferences and research papers have proliferated. International organisations such as the OECD and the EU issue regular reports. Population ageing is on every agenda, from G8 economic conferences to NATO summits. The World Economic Forum plans to consider the future of pensions and health care at its prestigious Davos conference early next year. The media, including this newspaper, are giving the subject extensive coverage.

Whether all that attention has translated into sufficient action is another question. Governments in rich countries now accept that their pension and health-care promises will soon become unaffordable, and many of them have embarked on reforms, but so far only timidly. That is not surprising: politicians with an eye on the next election will hardly rush to introduce unpopular measures that may not bear fruit for years, perhaps decades.

The outline of the changes needed is clear. To avoid fiscal meltdown, public pensions and health-care provision will have to be reined back severely and taxes may have to go up. By far the most effective method to restrain pension spending is to give people the opportunity to work longer, because it increases tax revenues and reduces spending on pensions at the same time. It may even keep them alive longer. John Rother, the AARP’s head of policy and strategy, points to studies showing that other things being equal, people who remain at work have lower death rates than their retired peers.

Magnum Photos

When the music stops much later

Younger people today mostly accept that they will have to work for longer and that their pensions will be less generous. Employers still need to be persuaded that older workers are worth holding on to. That may be because they have had plenty of younger ones to choose from, partly thanks to the post-war baby-boom and partly because over the past few decades many more women have entered the labour force, increasing

employers' choice. But the reservoir of women able and willing to take up paid work is running low and the baby-boomers are going grey.

In many countries immigrants have been filling such gaps in the labour force as have already emerged (and remember that the real crunch is still around ten years off). Immigration in the developed world is the highest it has ever been, and it is making a useful difference. In still-fertile America it currently accounts for about 40% of total population growth, and in fast-ageing western Europe for about 90%.

On the face of it, it seems the perfect solution. Many developing countries have lots of young people in need of jobs; many rich countries need helping hands that will boost tax revenues and keep up economic growth. But over the next few decades labour forces in rich countries are set to shrink so much that inflows of immigrants would have to increase enormously to compensate: to at least twice their current size in western Europe's most youthful countries, and three times in the older ones. Japan would need a large multiple of the few immigrants it has at present. Public opinion polls show that people in most rich countries already think that immigration is too high. Further big increases would be politically unfeasible.

To tackle the problem of ageing populations at its root, "old" countries would have to rejuvenate themselves by having more of their own children. A number of them have tried, some more successfully than others. But it is not a simple matter of offering financial incentives or providing more child care. Modern urban life in rich countries is not well adapted to large families. Women find it hard to combine family and career. They often compromise by having just one child.

And if fertility in ageing countries does not pick up? It will not be the end of the world, at least not for quite a while yet, but the world will slowly become a different place. Older societies may be less innovative and more risk-averse than younger ones. By 2025 at the latest, about half the voters in America and most of those in western European countries will be over 50—and older people turn out to vote in much greater number than younger ones. Academic studies have found no evidence so far that older voters have used their clout at the ballot box to push for policies that specifically benefit them, though if in future there are many more of them they might start doing so.

Nor is there any sign of the intergenerational warfare predicted in the 1990s. After all, older people themselves mostly have families. In a recent study of parents and grown-up children in 11 European countries, Karsten Hank of Mannheim University found that 85% of them lived within 25km of each other and the majority of them were in touch at least once a week.

Even so, the shift in the centre of gravity to older age groups is bound to have a profound effect on societies, not just economically and politically but in all sorts of other ways too. Richard Jackson and Neil Howe of America's CSIS, in a thoughtful book called "The Graying of the Great Powers", argue that, among other things, the ageing of the developed countries will have a number of serious security implications.

For example, the shortage of young adults is likely to make countries more reluctant to commit the few they have to military service. In the decades to 2050, America will find itself playing an ever-increasing role in the developed world's defence effort. Because America's population will still be growing when that of most other developed countries is shrinking, America will be the only developed country that still matters geopolitically.

Ask me in 2020

There is little that can be done to stop population ageing, so the world will have to live with it. But some of the consequences can be ameliorated. Many experts now believe that given the right policies, the effects, though momentous, need not be catastrophic. Most countries have recognised the need to do something and are beginning to act.

But even then there is no guarantee that their efforts will work. What is happening now is historically unprecedented. Ronald Lee, director of the Centre on the Economics and Demography of Ageing at the University of California, Berkeley, puts it succinctly: "We don't really know what population ageing will be like, because nobody has done it yet."

Sources and acknowledgments

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Offer to readers

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LinkedIn v freemasons

Joining the club

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Networking websites are booming, but they have not supplanted more traditional business networks

Eyevine

FRANÇOIS PÉROL, the adviser whom Nicolas Sarkozy, France's president, controversially appointed in February to head two merging mutual banks, is not known as a champion of transparency. But Mr Pérol has let it be known that he intends to reduce the influence of freemasons at Caisse d'Epargne and Banque Populaire. He has refused an invitation to a *tenue blanche ouverte*, a masonic meeting that non-freemasons may attend. And he does not want senior posts shared among the banks' various rival lodges.

French business may be particularly full of networks, but every country has its cliques, whether based on education, social background or spiritual beliefs. In Spain, Italy and Latin America as well as France, businesspeople speak of the influence of Opus Dei, a conservative Catholic lay order which supports a number of business schools. America has its Ivy League alumni groups and Rotary clubs. Chinese businesspeople often rely on *guanxi*, or personal connections.

At the same time online professional networks such as LinkedIn, headquartered in California, Viadeo, a French-owned website, and Xing, a site with a strong presence in German-speaking countries (formerly called OPEN Business Club), are surging in popularity, thanks in part to fear of lay-offs amid the recession. A year ago it took LinkedIn over a month to win 1m new members; it now takes about 15 days and the site has 42m members around the world. Online networks, in contrast to the old kind, are open to all and easy to join.

Old-style networks, however, are usually stronger than online ones, and the trust between their members facilitates transactions of all sorts. They can be particularly helpful for young companies in emerging markets. A study of entrepreneurship in China by Yusheng Peng of the Chinese University of Hong Kong, for instance, showed how kinship networks helped firms protect their property, obtain reliable information and identify opportunities. Social networks can also be speedier than formal systems: in July 2002, for example, when Vivendi, a French conglomerate, was weighed down with debt and needed to raise €3 billion (then $3 billion) in three days, its chief executive at the time, Jean-René Fourtou, turned to a group of bosses who were fellow rugby fans, including Claude Bébéar, then the chairman of the AXA Group, an insurance firm,

and the money was secured.

Some old-style networks aim to bring an ethical dimension to business. Not all students at IESE, a leading business school with campuses in Barcelona and Madrid, are aware that it is “an initiative” of Opus Dei. But many of them, particularly those of Spanish origin, are invited to join the order, says one graduate who was approached during his time there. IESE has a network of 15 business schools in developing countries, some of which explicitly state a goal of bringing a Christian perspective to business. Combining family with work, for instance, is the special subject of Nuria Chinchilla, a professor at IESE.

But networks can also have baleful effects. They sometimes abet crimes (see article). At French firms there is often pressure to hire or promote people based on their connections, businesspeople say. A study by Francis Kramarz and David Thesmar published in 2006 by the Institute for the Study of Labour in Bonn looked at three French business networks: former civil servants who graduated from the École Nationale d’Administration, former civil servants who graduated from the École Polytechnique and École Polytechnique graduates who went straight into business. These two elite schools, which produce 500 or so French graduates a year, dominate the boards of France’s biggest companies. The study showed that firms run by former civil servants who maintained their links to government markedly underperformed those run by executives with purely private-sector backgrounds.

Competition suffers, too. Nicolas Véron of Bruegel, a think-tank, says networks make it hard for new firms to emerge in France, since established ones are conservative about whom they do business with. As a result, he says, “you often see that successful young firms are business-to-consumer rather than business-to-business.”

On the face of it, networks are less important in more meritocratic America. Only 11% of bosses at big American firms received their undergraduate degrees from an Ivy League college, according to a survey last year by Spencer Stuart, an executive search firm. That suggests that performance matters more than the old school tie. But a 2007 study of mutual funds by Lauren Cohen and Christopher Malloy of Harvard University and Andrea Frazzini of the University of Chicago found that American fund managers invested more money in firms run by people who attended the same university as them. Moreover, membership of Rotary “service” clubs, which started in Chicago in 1905 and have since spread across the world, is by invitation only, and women were not admitted until the late 1980s. The Lions Club International, also based near Chicago, may be the most global offline business network, with 1.3m members in more than 200 countries. A third business network is the Benevolent and Protective Order of Elks, members of which must be Christians.

Will technology and globalisation undermine old networks? In some cases they are weakening. Swiss banks’ hierarchies, for instance, used to bear a resemblance to those of the country’s army, with strong connections between the two. But the network has largely disappeared, thanks to globalisation and a decline in the army’s role in society, says a Swiss banker. *Guanxi* are different from Western networks: they are much more personal, informal and subtle. Their importance is also diminishing as the Chinese economy becomes more market-oriented, says Derek Ling, founder of Tianji.com, a networking site owned by Viadeo.

“An active, open online network is far more competitive in today’s globalised business environment than local, closed networks such as alumni groups or freemasonry,” argues Reid Hoffman, founder of LinkedIn. Online networks’ most compelling advantage, in addition to openness and efficiency, is the chance they offer to connect across borders and among different sorts of people. Traditional networks, by contrast, tend to be strongest in domestic industries, such as construction. About two-fifths of LinkedIn’s members are female, whereas offline networks are usually dominated by men. And online networks include more entrepreneurs than traditional groups: they make up 30% of Viadeo’s subscribers, according to Dan Serfaty, the website’s co-founder.

Nevertheless, the old structures will not fall away soon. Indeed, Mr Serfaty argues that online networks can reinforce offline ones. A graduate of HEC (École des Hautes Études Commerciales de Paris) might use the school’s own website to look for any alumni working at, say, Google, he says. But using Viadeo’s tools, he can also do a broader search for anyone who attended HEC and knows someone working at Google, so the network becomes more powerful. Online networks make it easier to gather information on firms and their employees, argues Jean-Michel Caye, a specialist in human resources for the Boston Consulting Group in Paris. But if you want to influence a big decision or secure a job, he says, “it’s still the old networks that really count.”

Software that spots hidden networks

Electronic ties that bind

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Technology can help uncover dangerous cliques in companies

Illustration by Claudio Munoz

IT IS one of the more unusual cases that Elizabeth Charnock has worked on. Several years ago, Ms Charnock's software company, Cataphora, based in California, analysed the contents of e-mails sent by employees at a firm that had been sued by America's government for supposedly inflating charges on federal contracts. Cataphora's analysis helped to prove that the allegation was groundless. But it also revealed that some executives at the company shared an interest in bondage, lacing their e-mails to one another with references to their proclivity but making no mention of it in correspondence with other staff.

In this instance, the result was simply deep embarrassment. But other companies have ended up in serious trouble because of hidden networks. "In internal corporate investigations you often find informal cliques that communicate in ways designed to execute a fraud or to cover it up," says Robert Sherry, a partner at K&L Gates, a law firm. The recession increases the risk that such groups of rogue employees will be tempted to engage in wrongdoing to protect their jobs or bolster their finances.

At the same time, the volume of electronic communication is exploding, complicating efforts to spot misconduct. Forrester, a research firm, reckons corporate e-mail archives are growing by over 40% a year. The ability to identify internal cliques can keep legal bills down by allowing lawyers to spot potentially damaging activity fast. Firms that swiftly uncover and put a stop to wrongdoing might also get more lenient treatment from regulators if, say, their employees are found to have broken antitrust rules.

That is why firms such as Cataphora and RenewData that specialise in e-discovery—the practice of mining electronic records to unearth important data and relationships—are seeing healthy demand for their services. Cataphora's software lets firms analyse everything from e-mails to electronic calendars and thus build a picture of typical patterns of communication across their operations. It then flags exceptions to those patterns, such as individuals who send many messages to one another even though they are not in the same unit and have little reason to interact.

The software can dig deeper still by analysing linguistic patterns. In one case, Cataphora spotted a link between several executives at a firm that had been issuing bogus invoices to inflate its revenues. A program flagged that the executives, who were all in on the scam, had been using the same unusual sign-off phrase in their e-mails, which turned out to be associated with a college fraternity to which they had all belonged.

The recession hits Fininvest

Relegated

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Silvio Berlusconi's business empire faces leaner times

WHEN Silvio Berlusconi, Italy's prime minister, bought AC Milan, the football team he had supported as a boy, in 1986, it seemed a dream come true. But the team, for many years a force in European football, has had a disappointing run of late, failing to qualify for the 2008-09 Champions League of Europe's leading clubs and finishing the season far behind the winner of Italy's Serie A league.

Expensive but successful football clubs are one matter; costly also-rans, another. Last year AC Milan's losses shot to €68m ($100m) from €32m in 2007, and Fininvest, the Berlusconi family's holding company, which owns the club, has had to deny reports that it is selling its stake.

Not that losses at AC Milan put Mr Berlusconi's wealth at risk. Fininvest, of which Mr Berlusconi owns 63.3%, with the rest owned by his five children, reported net profits on June 18th of €242m for 2008 and cash holdings of €729m at year-end. It has large stakes in three listed firms: 38.6% of Mediaset, Italy's biggest private television firm; 50.1% of Mondadori, Italy's biggest book and magazine publisher; and 35.1% of Mediolanum, a financial-services group.

Mediaset controls Telecinco, a Spanish television company, but its main market is Italy, where its three channels won an audience share of 42% last year (6% more than the three channels of RAI, the state-owned broadcaster). Although Mediaset has tried to find new sources of revenue, it remains dependent on advertising, which accounted for 75% of total Italian revenues of €3.3 billion in 2008. (Telecinco's revenues were €982 million.) Advertising has withered in the recession, causing Mediaset's revenues to decline by 12% in the first quarter and its net profits by 50%.

The difficulties faced by Mondadori are complex and more intractable. The recession has led to reduced spending on books and magazines, and businesses have cut their advertising. It made a slender net profit of €97m on sales of €1.8 billion in 2008. At the end of April it decided that no dividend would be paid this year. Moreover, technological innovation is transforming the publishing industry at an accelerating pace. Last October Mondadori announced the sale of 80% of its printing arm and is looking to rationalise its business further.

The main businesses of Mediolanum, Fininvest's third pillar—banking, mutual funds and life insurance—have also been weakened by the global crisis. Between the end of 2007 and the end of last year, assets under its management in Italy fell from €27.4 billion to €23.9 billion while new insurance business slipped from €3.4 billion to €2.7 billion. Abroad, the contraction was even more severe: assets under management in Spain and Germany dropped from €2.7 billion to €1.7 billion. At €131m, net profit was down 38% last year.

Fininvest is paying for its recent conservatism. It got into television 30 years ago and moved into financial services not long after; Mondadori was acquired in 1991. But little has changed since except those firms' valuations. In April 2001, just before parliamentary elections that Mr Berlusconi won, Fininvest's stake in Mediaset alone was worth the equivalent of €6.8 billion. Its stakes in Mediaset, Mondadori and Mediolanum are now worth about €3.1 billion.

Fininvest notes that Mr Berlusconi is no longer directly involved in the holding company or its affiliates, but keeping Mediaset in friendly hands is crucial to his political ambitions. Marina Berlusconi, his eldest daughter, is now Fininvest's chairman and also heads Mondadori. Three more of his children hold board positions elsewhere in the group.

Fininvest paid dividends of €208m this year, about 16% less than last year, of which Mr Berlusconi received about €132m. That should provide some comfort amid the allegations of sexual indiscretions with which he

has been bombarded in recent weeks, prompting calls for his resignation (see article). Even if Mondadori fails to deliver the rich returns that it did before this year, the financial sector continues to suffer and increased competition cuts profits from television, Mr Berlusconi would still be able to scrape by in retirement.

Formula One's civil war

Mosley submits

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The car firms behind the big teams have taken the wheel at the racing series

Reuters

It was even messier at headquarters

IT WAS 11am in Paris, but high noon for Formula One racing. On June 24th at the grand headquarters of the Fédération Internationale de l'Automobile in the Place de La Concorde in Paris, its aristocratic president, Max Mosley, squared off against the small-framed, big-haired Luca di Montezemolo of Ferrari. Mr Montezemolo was threatening to take the big teams out of Formula One (F1), the world's leading motor-racing championship, and set up a rival series unless Mr Mosley accepted his demands.

Within two hours Mr Montezemolo had prevailed. Mr Mosley agreed to step down more or less immediately, his decision to impose a £40m ($66m) spending cap on teams participating in the championship was scrapped and the teams won a formal role in the governance of the sport. After several weeks' talk of the teams driving off, of lawsuits galore and, finally, of compromise, the clash ended in a rout.

For ten years the teams have sought a bigger say in F1. "We're tired of the present system. We want proper governance that is adhered to," said John Howett, head of Toyota's F1 team and vice-chairman of the Formula One Teams' Association (FOTA), on the eve of the showdown. "It is difficult to continue with Sir Max there." Mr Mosley's involvement in a much publicised sex scandal last year had done little to bolster his position.

Teams backed by big carmakers such as Toyota, Mercedes, BMW, Ferrari (part of Fiat) and Renault had grown frustrated at the autocratic way the sport was being governed by Mr Mosley and Bernie Ecclestone, two British racing veterans who have kept a tight grip on the rule-book and purse-strings of F1 for around 30 years. Firms founded by Mr Ecclestone control the sport's commercial affairs, including the lucrative sale of rights to stage races and to broadcast them. They receive over half the fees paid by broadcasters and the companies or governments that put on the races. The teams want a bigger share of the revenues, although the current arrangement will remain in place until 2012.

Another bone of contention is the decision about where the 17 races in each year's championship should take place. About half of them are still in Europe, but the season now stretches from Melbourne in March to Abu Dhabi in November, passing through China, Brazil, Japan and Malaysia on the way. The newer venues were added partly to broaden the sport's appeal but mainly because the promoters concerned have built fancy courses and paid lavishly for the privilege of staging races. Meanwhile France, the spiritual home of motor racing, and America, the most important car market in the world, have been struck off F1's calendar, to the carmakers' dismay.

The global recession caused the simmering discontent in the sport to boil over into open revolt. After rising costs forced Honda to drop out of F1 last December, Mr Mosley responded by capping the amount each team could spend at £40m a year, for fear that the smaller teams might disappear from the starting grid. Teams that agreed to the limit would be free to introduce any technical changes they dreamed up to improve their cars. Those that refused the cap would be subject to tough scrutiny and stricter technical rules—an intrusion the carmaking teams in particular resented. They wanted the freedom to spend as much as they liked and to innovate; they are, after all, in the sport to boost their image. So they threatened to set up an alternative championship under the auspices of FOTA.

Previous revolts had crumbled, most recently in 2005. But this week FOTA was confident it had lined up a credible series of races with enough circuits, famous drivers and loyal sponsors to threaten F1's monopoly.

In the event, the contingency plans were not needed. Mr Ecclestone seems to have deserted his old friend after FOTA won the backing of the ultimate authority in F1, the private-equity firm CVC Capital, which bought control of Mr Ecclestone's sports-rights company a few years ago. Its bankers had been worrying that the sport it had bought might fall apart. In the end, it was Mr Mosley and Mr Ecclestone's authority that collapsed.

Anglo American spurns Xstrata

Anglophilia, Xstrataphobia

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The latest proposal for a big mining merger runs into opposition

IN MINING, it seems, opposites do not attract. On Monday June 22nd Anglo American, a mining firm listed in London and Johannesburg, sent Xstrata packing, after the Swiss firm proposed a £40 billion ($65 billion) merger. Unlike its rivals, Anglo American has never gone through a transformative merger in its 90-year history. Xstrata, which was created in 2002 and has since gone through a series of medium-sized mergers, looks unlikely to change that. Its proposal, though billed as a merger of equals, looks like a takeover, with no premium for the sellers.

The two firms do have some things in common: both were of similar value before the approach became public, with comparable debts. The combination would be the world's biggest producer of diamonds, platinum, chrome and zinc, and the second-largest supplier of coal for steelmakers and copper. Xstrata puts potential annual savings from the merger at over $1 billion within three years. But Anglo dismissed the idea as "totally unacceptable" on the grounds that Xstrata's mines are not in the same league as its own low-cost, long-life assets. Xstrata disputes this.

Known for tightly controlling costs, Xstrata has outperformed Anglo of late. But Anglo reckons its share price will pick up as the price of platinum and sales of diamonds rebound. The first has been hit by dwindling car sales (it is used in exhaust systems), the second by diminished appetite for luxury goods in the recession. Anglo is touting its own cost-cutting plan that it says will save $2 billion by 2011.

Rumour also has it that Mick Davis, Xstrata's boss, would want to run the whole show. Xstrata hopes that Anglo's investors, miffed by some ill-judged acquisitions and the company's poor recent performance, will still see the advantage of harnessing Xstrata's expertise in cutting costs and put pressure on Anglo's managers to think again. Some hope for a sweetened offer, though Xstrata would have trouble finding the money.

Anglo's boss, Cynthia Carroll, clearly has no wish to be sidelined. In rebuffing Xstrata she has an ally in South Africa's government, which has a 5% stake in Anglo and a competition authority with the power to impede the merger. Anglo is regarded as a national champion, even though it moved its headquarters to London a decade ago. A third of its assets and shareholders remain in South Africa. The unions, important backers of the ANC, South Africa's ruling party, are fearful that jobs will go, though Xstrata believes that it can cut costs without firing any miners. And some suspect that Mr Davis would want to incorporate the new company in Switzerland, with its low taxes, rather than retain a listing in South Africa.

A few analysts regard Anglo's swift rebuff of Xstrata as a sign that China's Chinalco or Vale of Brazil may be poised to make a better offer. Firms with ties to China's government have been scouting enthusiastically for natural resources of late (see article). But if South Africa's government looks askance at Xstrata, it is even less likely to welcome a state-controlled Chinese firm or a Brazilian national champion.

Sinopec buys Addax

Bottom of the barrel

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A Chinese oil firm buys an exploration outfit willing to drill almost anywhere

Reuters

Controversy in the pipeline

MOST firms making an acquisition want, at the very least, to buy assets protected by strong legal systems in stable countries. But when it comes to buying natural resources, China's large state-controlled enterprises have found themselves blocked in whole or part from countries offering precisely those virtues because of concerns about their own operating practices. As a result, China's desperate hunt for energy to feed its vast industrial economy is focusing on trickier locations. On June 24th a subsidiary of the China Petroleum & Chemical Corporation (Sinopec) announced plans to buy Addax Petroleum, a Swiss company which has listings in Toronto and London and drilling rights in Iraq, Gabon and Nigeria.

The deal is worth $9 billion including the assumption of debt. If it succeeds (it has already been accepted by Addax's management), it will be the biggest takeover of a foreign firm by a Chinese one. Sinopec calls it "transformational", but in reality it is merely the latest and largest of many similar deals. In December, for example, another Sinopec subsidiary spent $2 billion to acquire Tanganyika Oil, which, like Addax, trades on the Toronto Exchange. Tanganyika produces 23,000 barrels a day, one-sixth of Addax's current production.

Before the Addax deal closes, Sinopec will need the approval of China's government (almost certain, given its clout) and of Addax's shareholders who, based on the large premium it offered to the share price, have little to complain about. Potentially more troublesome are the approvals that may be required in the various countries where Addax operates, and protests from human-rights activists, who have targeted Chinese firms working in Sudan and other unstable places.

Many of Addax's projects are controversial. Some of its drilling rights in Nigeria, for example, are in dispute. Its contracts in Iraq are with the government of the autonomous Kurdish area, and have been denounced by the oil minister in Baghdad. So the takeover may complicate Sinopec's efforts to win access to oil elsewhere in Iraq. The only certainty is that the deal will not quench the thirst of Sinopec and its fellow state-controlled oil firms, PetroChina and CNOOC, for foreign oil, whatever the risks.

GE and industrial loan companies

Parting company

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Will the Obama administration's reforms of the financial system hurt retailers and manufacturers with lending arms?

THE talk had become so fevered that on June 22nd Jeffrey Immelt, General Electric's embattled boss, sent out a memo to all staff to quash it. "GE is and will remain committed to GE Capital," he insisted. These words of reassurance were prompted by the financial-reform plan the Obama administration had unveiled earlier in the month, which many saw as heralding the dismemberment of America's biggest conglomerate, with interests from nuclear power to financial services.

GE is not the only company in the line of fire. An array of retailers and manufacturers that provide customers with loans for purchases, from Target to Harley-Davidson, also face threats to their business if the proposed legislation makes it through Congress. That, as Mr Immelt pointed out in his memo, is a big if: "it is very early in the process, and Congress will now spend months reviewing and drafting legislation". During that period, GE will doubtless deploy its huge lobbying clout to argue that it should be left alone.

The administration's proposals pose two main concerns for GE, of which much the greatest is the implication that GE Capital, the firm's vast finance arm, would be considered a "Tier 1" bank, meaning one that is so big and systemically important that it should be subjected to especially thorough scrutiny and tight controls. Restrictions on the industrial activities of such banks might force it and the rest of GE to part company.

Mr Immelt rejects this prescription on the grounds that the combination of commerce and finance within the firm played no part in the financial crisis. Indeed, GE argues that the strong cashflow from its industrial businesses—aircraft engines, power-supply equipment and so forth—actually protected its financial operations during the credit crunch, when stand-alone financial firms suddenly found they could no longer raise funds.

But GE did have difficulties raising money, which led it to turn in October for (expensive) help to Warren Buffett, a celebrated investor. The firm says it did not need assistance obtaining short-term commercial loans, and only took part in the Federal Reserve's emergency scheme to provide such lending to demonstrate its support for the concept. But its struggles certainly added to the general sense of panic at the time. Had GE failed, it would have done significant damage to the financial system and the wider economy. If companies such as General Motors and Chrysler are "too big too fail", then so is GE Capital, let alone the conglomerate as a whole. And it makes little sense to regulate GE Capital differently from any other big, risk-taking financial business.

Getty Images

A bank in disguise

It is not clear, however, that GE's industrial businesses added to the systemic risk posed by GE Capital, or to the difficulty of regulating it. Nevertheless, given the way the political wind is blowing, GE Capital should expect to feel a heavier regulatory hand on its shoulder in future. It is also likely that GE Capital will find it more expensive to borrow for some time to come. That may well make being in financial services less attractive to its shareholders, who have already successfully pressed for a paring down of GE Capital, partly in response to the firm's plunging share price during Mr Immelt's eight-year reign. Some want GE to get out of finance altogether.

GE is also concerned, along with a host of other companies, about the administration's proposal to put an end to a category of financial firm they have all set up called an "industrial loan company" (ILC). These are state-regulated outfits, based mainly in Utah, which can take in federally insured deposits from savers, make loans and issue credit cards, but are subject to less onerous regulation than banks. They have proliferated in recent years as non-financial firms such as Target, BMW, Pitney Bowes and UnitedHealth have created ILCs as a cheap and profitable way to steer credit and other financial services to their customers.

The administration wants to subject all consumer-finance firms to the same regulations to prevent a gradual migration to the most lax form of oversight. That fear is not unreasonable, and the response sensible enough. But it is likely to be undermined by the boundless ingenuity of businesses looking for a way around supposedly comprehensive regulations. Moreover, there is no evidence that the ILCs of non-financial companies played any part in the financial crisis, or that they pose any systemic risk.

Harley-Davidson lending money to fifty-somethings in the midst of mid-life crises so that they can buy its "hogs" is unlikely to bring capitalism to its knees. Indeed, since the 19th century, when firms such as Singer started extending "dollar down, dollar a week" loans to help people buy sewing machines, such financing has been a routine feature of business life. It is unlikely to go away even if regulation makes it more expensive. Instead, those firms that depend on providing such loans will presumably accept the stricter oversight that comes with owning a bank.

The bankers of Bentonville

The crackdown on ILCs, more than anything, is testimony to the phenomenal lobbying power of America's banks, which have long railed against the growth of cheaper, more lightly regulated competitors. Back before the financial crisis, the banks protested so furiously against an attempt by Wal-Mart to obtain a licence to start its own ILC that the giant retailer backed down. But whatever the regulatory category, the sort of competition that a firm as large and well-run as Wal-Mart would bring to consumer banking might be just what bloated incumbents such as Citigroup desperately need.

Face value

Mr Clean

Jun 25th 2009
From The Economist print edition

Ian King wants to transform the way the world's third-biggest defence company does business

BAE Systems

ON JUNE 27th last year, just six weeks after Mike Turner, the chief executive of BAE Systems, had been detained on arrival in America in connection with corruption allegations, Ian King was announced as his successor. Mr Turner and another of the firm's directors were not held for long, and many felt that the Department of Justice, which seized their laptops and BlackBerrys, had acted heavy-handedly. But the incident, which stemmed from a long-running investigation into claims that BAE had lubricated the £43 billion ($70 billion) "al-Yamamah" arms deal with Saudi Arabia with bribes to government officials and members of the royal family, was yet another embarrassment for the world's third-biggest defence company.

In some ways Mr King's appointment was a surprise. Dick Olver, BAE's chairman since 2004, has been on a mission to restore the reputation of a firm that has all too often found itself at the centre of corruption allegations. In 2007 he took the extraordinary step of asking a former Lord Chief Justice, Lord Woolf, to lead an independent inquiry into BAE's ethical standards. After he pushed Mr Turner into early retirement, it was assumed that Mr Olver would make a clean break with the past by choosing an outsider to carry forward his crusade. Indeed, several Americans were considered for the job (America is the British firm's biggest market). So when Mr King, the only internal candidate, got the nod, some suspected that the British government had used its "golden share" to veto the appointment of a foreigner.

BAE executives deny that happened, but the government must have been relieved that the country's dominant defence contractor would be run by someone it knew well. Mr King began his career in 1976 as a trainee accountant with Marconi, a defence-electronics subsidiary of Arnold Weinstock's GEC, Britain's biggest industrial conglomerate. In the late 1990s a wave of consolidation hit the defence industry on both sides of the Atlantic and Marconi Electronic Systems, as it had become, was taken over by British Aerospace to form BAE Systems.

John Weston, the abrasive boss of British Aerospace asked Mr King, who had been finance director at Marconi for several years, to handle strategy for the merged firm. A number of operational roles followed, which ultimately left Mr King running most of the business outside America. Mr King's background at Marconi may well have counted in his favour when it came to appointing a new chief executive. British Aerospace, which did the first al-Yamamah deal in 1985, had a buccaneering culture very different from that of GEC, where, says Mr King, Lord Weinstock always demanded the highest standards of commercial behaviour.

After nearly a decade of steadily growing profits and armed with a strong balance-sheet, BAE is in many ways in good shape. But the next few years are likely to be more testing. With the exception of Saudi Arabia, where the firm has recently completed another multi-year deal to sell and maintain fighter aircraft, BAE's major customers are pulling in their horns. Spiralling government debt in America and Britain means that "wars of choice" are no longer affordable and the search is on for cuts in big procurement programmes. The review recently undertaken by Robert Gates, America's defence secretary, resulted in the cancellation of part of the Future Combat Systems programme, a big army-modernisation project for which BAE is a prominent contractor. In Britain, cuts to an already overstretched defence budget are only being postponed until after next year's election.

Mr King appears unfazed. BAE is less dependent on big "platform" sales than it used to be and now sees itself as a provider of "through-life support" for complex systems, much like the aero-engine industry. He also believes that BAE's strength in army equipment, particularly armoured and mine-resistant vehicles, stands it in good stead for what he calls the "current fight" in places such as Afghanistan. It is all business as usual for an experienced operator like Mr King. What is not, however, is the company's effort to transform the way in which it does business. BAE admits to no wrongdoing over al-Yamamah, which was primarily a deal between governments, it says, nor over any of the other deals that are still under scrutiny (in 2007, the British government said BAE contracts in six countries were being investigated by the Serious Fraud Office). But BAE has promised not just to implement the 23 recommendations made by Lord Woolf in his report, but also to "embed" his ideas in its culture. To that end, Mr King has embarked on a huge training programme to inform all 97,000 BAE employees worldwide of their ethical responsibilities.

1-800-MORAL-FIBRE

Mr King says he wants staff to be able to raise ethical issues in the same way they would an engineering problem—something to be discussed openly. Earlier this year BAE sent a 64-page code of conduct to each of its workers, with detailed advice on how to behave in every situation. With the booklet came a small card, to be carried at all times, with a list of toll-free numbers for the firm's "ethics helpline".

It is easy to scoff at the idea of an arms firm preaching ethics, particularly one that is still making money from deals concluded before its squeaky-clean rules were put in place. Nor is an industry veteran, such as Mr King, an obvious new broom. But he has all the fervour of a true convert. "You have to believe in it," he says. "It's a journey you personally have to make." Helpfully, a significant part of his own remuneration is, he says, linked to making BAE "a benchmark" for responsible behaviour in the industry. Shareholders, he claims, are supportive. They have accepted that it is better to lose business in some parts of the world than to expose BAE to reputational risk. As for the Saudis, Mr King says that they too now want to do things differently. And if a rival firm were to offer to do business with them in the "traditional" way? "Then the Saudis will have to make their choice," he says.

Reforming American health care

Heading for the emergency room

Jun 25th 2009 | WASHINGTON, DC
From The Economist print edition

America's health care is the costliest in the world, yet quality is patchy and millions are uninsured. Incentives for both patients and suppliers need urgent treatment

Illustration by Otto Steininger

NO ONE will be astonished to hear that health care costs more in Indiana than in India. However, a few might be surprised to learn that Americans spend more than twice as much per person on health care as Swedes do. And many may be shocked to be told that in Miami people pay twice as much as in Minnesota, even for far worse care.

The American health-care system, which gobbles up about 16% of the country's economic output, is by far the most expensive in the world (see chart 1). The Congressional Budget Office (CBO) estimates that on current trends spending on Medicare and Medicaid, the government schemes for the old and the poor, will rise from 4% of GDP in 2007 to 12% in 2050. The prospect of long-term fiscal disaster is the main reason why efforts to reform health care are gaining momentum in Washington, DC. As Peter Orszag, the director of Barack Obama's Office of Management and Budget, puts it, "that 'long term' keeps getting closer and closer."

The system has its defenders. They point out that countries should expect to spend more on health care as people age. Americans are wealthy enough to choose extra health care over other things. Their free-spending approach calls forth the invention and speedy adoption of valuable new drugs, devices and procedures, whereas Europe's stodgy and stingy (not to mention socialist) health-care systems deny coverage and ration care, to the detriment of their people's health.

A poll carried out for *The Economist* by YouGov highlights Americans' beliefs about the state of their system. Although 68% of them rate the care they receive as "excellent" or "good", 52% are dissatisfied with the quality in the country as a whole. Only 25% think the system works pretty well and requires only minor changes; 40% think fundamental change is needed and 29% think it should be completely rebuilt. Some results are shown in chart 2. A fuller version is available at www.economist.com/yougovpoll.

The doubters have a better case than the defenders. Granted, medical inventions are readily embraced by American doctors and patients. In specific instances—technology to save babies born prematurely and statin drugs to reduce cholesterol, to take two—the benefits of spending greatly outweigh the costs. But if the system in general were providing value for money, America's vast expenditure would at least be reflected in a healthier population than in more frugal countries.

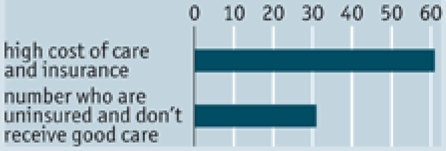
Alas, it is not. Comparisons with other rich countries and within the United States show that America's health-care system is not only growing at an unsustainable pace, but also provides questionable value for money and dubious medical care. Three troubling symptoms stand out: uneven quality of care, inadequate coverage and soaring costs.

Questions of health 2

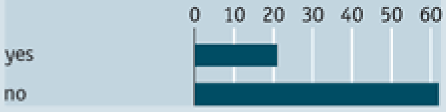
Overall, do people like you get better or worse health care in the following countries than in the United States? % replying:

	better	same	worse	don't know
Canada	32	12	25	31
Britain	24	11	24	41
Japan	19	13	14	53
Mexico	8	6	49	37
France	22	13	19	46
Germany	22	12	16	50

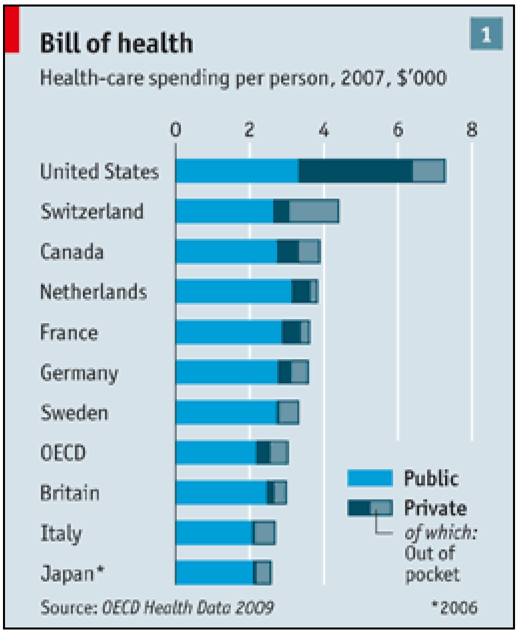
When it comes to health care, what do you think is the bigger problem? % replying:



Would you support a health-care reform plan if it required you personally to pay more for your health insurance or raised your taxes? % replying:



Source: *The Economist*/YouGov Poll



Start with quality. Evidence is mounting that spending more does not necessarily buy better health. On the contrary, it appears that many Americans are getting mixed or even downright dreadful health care. In a recent study economists at the OECD found that America does indeed do well on some measures, such as breast-cancer survival rates and cervical-cancer screening, compared with other rich countries. However, it does worse in other areas. American infant mortality was 6.7 per 1,000 births in 2007, against an OECD average (excluding Mexico and Turkey) of 4.0. The death rate after haemorrhagic strokes was 25.5% in American hospitals but only 19.8% in OECD countries as a group.

Jonathan Skinner, an economist at Dartmouth College, cautions that factors other than health-care systems—attitudes to teenage pregnancy, say, or smoking—may influence the numbers. Even so, he thinks the system is wasteful. In a paper in the *Journal of Economic Perspectives* last year he and Alan Garber, of Stanford University, argued that America's health system was "uniquely inefficient", producing too little per unit of input and consuming far too much of the country's resources.

Mr Skinner is involved with another worrying line of research. The Dartmouth Atlas project has scrutinised variations in health outcomes and spending involving Medicare. It has found wide differences in costs across the country—less than $5,000 per person in Salem, Oregon, in 2006; a bit more than $8,000 in San Francisco, in line with the national average; more than $16,000, and rising fast, in Miami—but no connection between higher spending and better outcomes. In fact, the evidence points in the other direction: outcomes tend to be better where costs are lower. Mr Orszag points to the Dartmouth work to argue that up to 30% of America's health-care spending is sheer waste.

The second symptom is coverage. Uniquely among rich countries, America's system of health insurance is not universal. Around 49m people have no health insurance. On current trends, within a decade 60m will be without cover. Studies have shown that not all these people are indigent: a quarter or more can afford insurance, but choose not to buy it.

They know they are unlikely to be left to die in the streets. With the truly poor, the free-riders turn up at emergency rooms. This is hugely inefficient, because pricey late interventions and operations could very

often have been avoided with a much smaller investment in preventive care. Insured people and taxpayers are forced to cross-subsidise such “uncompensated” and wasteful treatments to the tune of tens of billions of dollars per year.

Other rich countries cover almost all their citizens in one of two ways. Some, such as Britain, Canada and Sweden, have “single payer” systems, in which taxes support a public service. Others, notably the Netherlands and Switzerland, oblige individuals to buy insurance. France has a mixed public-private system.

After decades of failed attempts at reform, a consensus appears to be emerging in America around the principles needed for universal coverage. One likely change means a restructuring of America’s failed health-insurance markets. Firms are today allowed to pick the safest patients and reject the sickest. In future they will have to take all comers. Because this imposes unfair burdens on firms that attract lots of older or sicker people, reform is likely to include government-funded mechanisms for risk pooling or reinsurance. The Netherlands, in particular, uses such an approach.

American health insurers, having long opposed this idea, have performed a startling U-turn in recent weeks. America’s Health Insurance Plans, their chief lobbying group, now says it is willing to accept such heavy-handed reforms—if they are accompanied by a requirement that all Americans purchase coverage. This may seem a cynical ploy to expand their business, but some compulsion is needed to get around the selection problem. Any legislation is likely to include subsidies to help the poorest pay for cover.

If done properly, this will in time move America towards the Swiss and Dutch models of universal private insurance. These are not perfect, to be sure. Regina Herzlinger of Harvard Business School observes that the Dutch reforms have led to rapid consolidation of insurers and hospitals, fuelling resented price increases. She favours the decentralised Swiss model, which preserves individual choice and competition. Others note that Swiss health-care costs are high by European standards. But they are a third less, as a share of GDP, than America’s, and the country’s excellent health outcomes should be the envy of American reformers. Our poll suggests that an individual mandate would be unpopular, with only 21% in favour and 53% opposed. Respondents did favour having the option to buy from the government, by 56% to 23%.

Such reforms would expand coverage, but could exacerbate the third symptom, cost, as the experience of Massachusetts, a trailblazing state that has already implemented a plan for universal coverage, suggests. The state faces possible bankruptcy unless it finds a way to rein in costs.

Your money or your life

Indeed, tackling inflation in American health care remains the most important and difficult part of the treatment. According to our poll, cost is a tender nerve: 61% thought the high cost of care and insurance was a bigger problem than the number of uninsured, against 31% who believed the reverse. Only 21% would be willing to support a reform plan if they had to pay more in insurance or tax; 62% would not.

Some common diagnoses are wide of the mark. One is price gouging by drug companies. In fact, pills account for barely a tenth of health-care spending in America and similarly small shares elsewhere. But aren’t costs lower in Europe because of price controls? Europe does indeed spend less on new branded drugs, but also uses fewer generic drugs and pays much more for them. And Switzerland actually has higher drug prices than America (as does Canada). Greedy drugmakers are not the main cause of America’s runaway costs.

Nor are baby-boomers, though they are often blamed for health-care inflation because there are a lot of them and they are getting old. Ageing will clearly push up costs in time (see our special report in this issue), but it is not the main culprit yet. The CBO estimates that ageing accounts for only a quarter of the health-care inflation to come in the next few decades, and the share in other rich countries is similar.

Doctors’ generous pay is another popular culprit. But doctors in several European countries are well paid too. The OECD estimates that general practitioners in America earn 3.7 times the average wage. Their British counterparts earn 4.2 times their national average. American specialists earn 5.6 times the average wage, against 7.6 times for their Dutch colleagues. Yet health-care costs in Britain and the Netherlands remain lower than America’s. The real problem is not how much American doctors are paid, but how. The system of medical reimbursement warps incentives for doctors, insurers and patients that lead Americans to consume more and more medical services. There is strong evidence that Americans use pills,

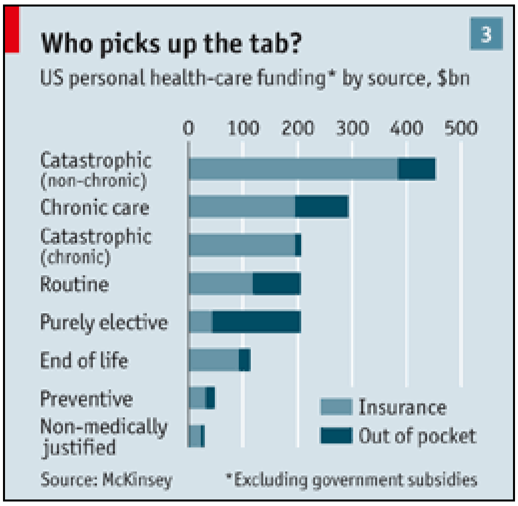
procedures, scans and other expensive forms of health care more often than do patients in other rich countries, and not always to good effect.

America's insurance system encourages overuse in several ways. One is the tax break that favours health insurance provided by employers, which leads to excessively generous coverage and hence over-consumption. Another is the fact that American health insurers earn a lot of revenue from administering the health plans provided to employees by big corporations which, in effect, insure themselves. This leaves insurers with no incentive to curb costs, because more spending means fatter management fees.

The incentives facing doctors are even more perverse. Most doctors are not paid a fixed salary, still less rewarded for better health outcomes. Integrated American systems such as Kaiser Permanente and the Mayo Clinic are exceptions to this rule, and Britain's National Health Service (NHS) is trying to adopt a similar approach. But most doctors and hospitals are paid more if they provide more services, regardless of the results. Predictably, this leads to far higher rates of doctors' visits, specialist referrals, scans and so on.

For instance, the OECD countries have an average of 11 magnetic-resonance imaging machines per 1m people. America has 25.9. America uses them more often, too: 91.2 times per 1,000 people per year, compared with the OECD average of 39.1. Similar tales can be told about other pricey kit.

This incentive problem even extends to patients. If patients pay very little out of their own pockets they have little desire to curb consumption. Though this is a problem in many OECD countries, in America the proportion of out-of-pocket spending has declined sharply in the past few decades. And a new report by McKinsey, a firm of management consultants, identifies a more subtle problem. Having examined insurance and out-of-pocket spending for several health risks, it concludes that Americans are generally "over-insured and under-saved". It is prudent for individuals to have comprehensive health insurance against catastrophic health risks such as heart attacks or cancer. But McKinsey finds that Americans with private health insurance often have generous coverage for non-essential and even medically unjustified care (see chart 3). This encourages over-consumption.



The power of sunshine

A second big factor pushing up health costs is the lack of competition among operators of American hospitals. Thanks to a wave of consolidation in recent years, argues Harvard's Ms Herzlinger, "most parts of the United States are dominated by oligopolistic hospital systems." George Halvorson, who heads Kaiser Permanente, insists that "there is an almost total lack of price competition among providers."

Nimble upstarts and innovators are challenging the incumbents in some areas. Such efforts range from specialist heart hospitals, which get better outcomes at more reasonable prices than local general hospitals, to retail clinics at Wal-Mart stores. Remote medicine, in the form of technology for tele-care or medical tourism to Thailand and Costa Rica, also poses a threat. But medical lobbies are using political influence and outdated regulations to thwart competition where they can (for example, through rules preventing a doctor from treating a patient in another state).

To counter this, reforms could allow federal regulators to overrule state-level obstacles to entrants such as clinics staffed by inexpensive nurse-practitioners. More transparency would help too, by empowering patients to choose hospitals and doctors providing good value and better results. Electronic medical records would make shopping around easier.

Another useful way to promote transparency and value would be to evaluate the cost-effectiveness of new drugs, devices and treatments. This may be common sense, but it is rarely done in America. Britain's National Institute for Health and Clinical Excellence (NICE) pioneered this approach, and other European countries have followed it. Andrew Dillon, the agency's chief executive, accepts that "the NICE model is not transportable in precise form" but he still insists that "one can dissect and apply what is relevant to other countries."

In America, the drugs and devices lobbies are violently opposed to a

Illustration by Otto Steininger

NICE-style agency that could issue mandatory rulings. They paint a scary picture of Americans being denied access to life-saving new drugs by faceless bureaucrats. In Britain NICE has come under fire for rulings that limited access to expensive drugs for Alzheimer's and cancer on the NHS. America could get around this problem by requiring and perhaps even funding studies, but leaving insurers and individuals to decide whether to pay for treatments.

More competition and transparency would help, but the main goal of any reform plan must be to address the perverse incentives that encourage overconsumption and drive up costs. Medicare has been tinkering with "pay for performance", a promising experiment. Mr Halvorson insists that by rejigging incentives other health providers can also create their own "virtual Kaisers".

If American reformers doubt the power of incentives, they should visit Sweden. Like other relatively cheap OECD systems, Sweden's single-payer model has been plagued by long waiting-lists—a sign, to American conservatives, of the rationing that goes with socialised medicine. Swedish health officials tried and failed to cut queues by increasing direct funding for hospitals and even issued an edict requiring hospitals to cut queues for elective operations to three months. Then, last year, the health ministry said it would create a fund into which it would pay SKr1 billion ($128m) a year for local authorities that managed to reduce waiting times to that threshold. Nine months ago virtually none of the counties passed, but this month the health minister revealed that nearly all had cut their queues to three months or less.

Anders Knape, the head of the organisation representing county governments, ascribes this to "a dramatic change in incentives". In the past, he explains, hospital bosses believed waiting lists were a sign of being overloaded, so they tolerated them in the hope of winning more funding. With the new scheme, however, "no queues means more resources".

If getting incentives right can mobilise even a state-run health system like Sweden's, surely there is scope for such reforms to fix America's mess too. If the United States couples its efforts to expand coverage with such a radical restructuring of the underlying drivers of cost inflation, there is every reason to think its health system can become the best in the world—and not merely the priciest.

Consumer spending in Asia

Shopaholics wanted

Jun 25th 2009 | HONG KONG
From The Economist print edition

Illustration by S. Kambayashi

Can Asians replace Americans as a driver of global growth?

ASIA'S emerging economies are bouncing back much more strongly than any others. While America's industrial production continued to slide in May, output in emerging Asia has regained its pre-crisis level (see chart 1). This is largely due to China; but although production in the region's smaller economies is still well down on a year ago, it is rebounding in those countries too. Taiwan's industrial output rose by an annualised 80% in the three months to May compared with the previous three months. JPMorgan estimates that emerging Asia's GDP has grown by an annualised 7% in the second quarter.

Asia's ability to decouple from America reflects the fact that the region's downturn was caused only partly by the slump in American activity. In most Asian economies falling domestic demand was more important than the drop in net exports in explaining the collapse in GDP growth. The surge in food and energy prices in the first half of 2008 squeezed profits and spending power. Tighter monetary policy aimed at curbing inflation then further choked domestic demand.

The recent recovery in industrial production reflects the end of destocking by manufacturers as well as the large fiscal stimulus by most governments. But the boost from both of these factors will fade. Meanwhile, export markets in developed economies are likely to remain weak. So the recovery in Asian economies will stumble unless domestic spending, notably consumption, perks up.

Consumers' appetite to spend varies hugely across the region. In China, India and Indonesia spending has increased by annual rates of more than 5% during the global downturn. China's retail sales have soared by 15% over the past year. This overstates the true growth rate because it includes government purchases, but official household surveys suggest that real spending is growing at a still-impressive rate of 9%. In the year to May, sales of household electronics were up by 12%, clothing by 22% and cars by a stunning 47%.

Elsewhere in the region, spending has stumbled, squeezed by higher unemployment and lower wages. In Hong Kong, Singapore and South Korea real consumer spending was 4-5% lower in the first quarter than a year earlier, a much bigger drop than in America. But Frederic Neumann, an economist at HSBC, sees tentative signs that spending is picking up. Taiwan's retail sales rose in May for the third consecutive month. Department-store sales in South Korea rose by 5% in the year to May.

It is often argued that emerging Asian economies have large current-account surpluses—and are thus not pulling their fair weight in the world—because consumers like to save rather than spend. Yet this does not really fit the facts. During the past five years consumer spending in emerging Asia has grown by an annual average of 6.5%, much faster than in any other part of the world. It is true that consumption has fallen as a share of GDP, but that is because investment and exports have grown even faster, not because spending has been weak. Relative to American consumer spending, Asian consumption has soared (see chart 2).

In most Asian economies, private consumption is 50-60% of GDP, which is not out of line with rates in countries at similar levels of income elsewhere. China, however, is an exception. Private consumption there fell from 46% of GDP in 2000 to only 35% last year—half that in America. In dollar terms, spending is only one-sixth of that in America. (Singapore's consumption is also low, at just under 40% of GDP.)

This explains why China's government has recently taken bolder action than others to boost consumption. Over the past six months the government in Beijing has introduced a host of incentives to encourage households to open their wallets. Rural residents get subsidies for buying vehicles and other goods such as televisions, refrigerators, computers and mobile phones; urban residents get a subsidy if they trade in cars and home appliances for new goods; tax rates on low-emission cars have also been cut. There is huge potential for higher consumption in the countryside as incomes rise: only 30% of rural households have a refrigerator, for example, compared with virtually all urban households.

The government has also introduced several measures this year to improve the social safety net, such as spending more on health care, pensions and payments to low-income households. On June 19th it ordered all state-owned firms that had listed on the stockmarket since 2005 to transfer 10% of their shares to the National Social Security Fund to shore up its assets. The short-term impact is likely to be modest but if such measures ease households' worries about future pensions and health care, it could in the long term encourage them to save less and spend more.

Another way to boost consumption is to make it easier to borrow. In most Asian economies household debt is less than 50% of GDP, compared with around 100% in many developed economies; in China and India it is less than 15%. South Korea is the big exception: households have as much debt relative to their income as Americans and their saving rate has fallen over the past decade from 18% of disposable income to only 4%. In many other Asian economies financing for consumer durables is virtually nonexistent. Promisingly, the Chinese bank regulator announced draft rules in May to allow domestic and foreign institutions to set up consumer-finance firms to offer personal loans for consumer-goods purchases.

These measures are a modest step in the right direction. But a bigger test of Asian governments' resolve to shift the balance of growth from exports towards domestic spending is whether they will allow their exchange rates to rise. A revaluation would lift consumers' real purchasing power and give firms reason to shift resources towards producing for the domestic market. But so far, policymakers have been reluctant to let currencies rise too fast.

Asian spending is already an important engine of global growth. Even before the crisis, emerging Asia's consumer spending contributed slightly more (in absolute dollar terms) to the growth in global demand than did America's. But it could be even bigger if Asians enjoyed the full fruits of their hard labour, rather than subsidising Western consumers through undervalued currencies. It is time for an even greater shift in spending power from the West to the East.

Buttonwood

Tied to the mast

Jun 25th 2009
From The Economist print edition

Coping with the politics of austerity

Illustration by S. Kambayashi

TAXES are unpopular, and so are public-spending cuts. Democracies may thus have an innate tendency to run up budget deficits. How to control the politicians' urge to splurge? In Greek mythology the song of the Sirens was so seductive that enraptured sailors let their ships run on to the rocks. Odysseus stopped his sailors' ears with wax and had himself tied to his ship's mast so he could hear the song without endangering his vessel.

Various attempts through history have been made to tie politicians to the mast and prevent them from ruining the public finances. The gold standard was one. By anchoring the value of money, the rights of creditors were protected. Spendthrift governments were forced to cut back.

But the gold standard and its successor, the Bretton Woods system, eventually fell apart. In their place came the "bond-market vigilantes". The idea was that investors would boycott the debt issues of offending countries and force governments to bring fiscal policy back into line. That discipline was undermined by the investment policies of Asian and Middle Eastern central banks, which recycled their surpluses into government bonds and kept countries' cost of borrowing down.

Now German politicians are attempting to impose their own discipline. In May they voted to restrict the ability of the federal government to run deficits of more than 0.35% of GDP from 2016. Compare that with a forecast deficit of 6% (including the Länder) next year. Even though the rule distinguishes between structural and cyclical deficits, it could still require Germany to raise taxes and slash spending in a recession—the mistake governments made in the early 1930s.

Perhaps the proposal will not stick. After all, the Gramm-Rudman-Hollings Act of 1985, designed to balance the American budget, was eventually overridden. And just look at California to see how well-meaning measures can lead to fiscal disaster. A two-thirds majority in the state legislature is needed to change taxes, and voters have used their referendum powers to block reforms. The result is that the state is drifting towards bankruptcy. Moody's warned on June 19th that it may downgrade California's credit rating by several notches, which could turn America's most populous state into a junk-bond issuer.

The California example is a sharp rejoinder to the superior attitude taken by Americans and Europeans during the Latin American and Asian crises of the 1980s and 1990s. Developing countries, it was assumed, were simply too immature to take control of their finances. But developed-country voters may be equally unwilling to swallow the medicine of austerity.

The politicians best placed to tackle their deficits may be those that are relatively free of legal restraint. In Britain, which has been described as an "elective dictatorship", the next government, likely to be the Conservative party, will inherit a fiscal mess. But it will be able to slash spending and raise taxes without hindrance, albeit at the cost of staggering unpopularity.

To switch from Greek myth to Roman history, this might be called the Cincinnatus approach, after the Roman general who was summoned from his farm to deal with enemy attack and returned to the plough once his duty was done. The Conservatives can do the right thing, at the cost of being a one-term government. The temptation, of course, will be to fudge the choice: announce a plan to cut waste in public spending, raise a few stealth taxes and hope that the economy recovers sufficiently to solve the problem.

But this crisis may be different. First, tax revenues seem to have become very volatile. This may be due to economies' dependence on the financial sector and the taxes on traders' bonuses, investment-bank profits, capital gains on rising stockmarkets and all the rest. The shrinking of the financial sector may have caused a permanent dent in the public finances. Second, the long-term fiscal problems of ageing populations (health care, pension costs) will start to make themselves felt over the next decade.

It is true that governments have recovered from enormous deficits in the past, notably after large wars. But post-war economies have a natural tendency to rebound, as soldiers return to more productive work, factories switch from making tanks to building cars, and so forth. No such automatic boosters will kick in this time. The kind of patriotic spirit that encourages consumers to put up with austerity is not yet in evidence either. There could instead be a long decade of political turbulence as voters find that the champagne has run out, and all they have left to drink is castor oil.

Economist.com/blogs/buttonwood

Chinese IPOs resume

Thirst-quenching

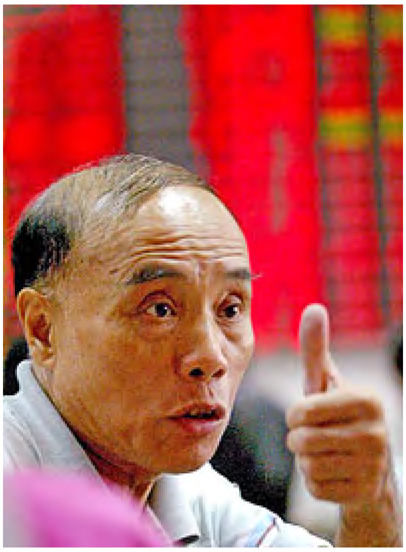
Jun 25th 2009 | HONG KONG
From The Economist print edition

After a long period of inactivity, China's equity market reopens

IT IS like a downpour after a drought. In 2007 and early 2008, hundreds of Chinese companies worked feverishly with accountants and bankers to prepare for initial public offerings. Their work came to nothing. Collapsing share prices, a contracting economy, unrealistic expectations on the part of sellers and, finally, restrictions from regulators crushed the IPO market. Now the companies and bankers that have managed to survive a brutal year are once again seeking capital, through listings on bourses in the mainland and beyond.

The first raindrop in China has been Guilin Sanjin, a manufacturer of Chinese medicine, which is expected to issue shares on June 29th on the Shenzhen Stock Exchange, the market for the country's smaller companies. The size of the offering is likely to be a bit under $100m—a mere rounding error compared to the mega-deals of two or three years ago, but a sign, nonetheless, that business has resumed.

AFP



He's in

Another 30 companies have reportedly received regulatory approval to list and have begun final preparation and marketing; 400 more sit in a queue waiting to be approved. Several state enterprises that went public on offshore markets, including China Mobile and CNOOC, an oil firm, are also expected to list at some point in Shanghai. So too may a handful of non-Chinese companies, with interest already expressed by HSBC, in deference to its Shanghai roots, and the New York Stock Exchange (NYSE).

In Hong Kong, a few companies did manage to float in the past few months but the going was tough, with price estimates cut repeatedly prior to the offering, buyers corralled from friends, families and affiliates, and a lacklustre aftermarket. Conditions have turned. Many of these deals are now up significantly. Three small companies have gone public since June 16th, with shares in each case rising by at least 20%.

Bawang, a Chinese toiletries company, is in the final stages of a roadshow and appears likely to price at the top of its pre-marketing estimate. More sizeable deals are expected by the year's end, including a listing of the Asian life-insurance operations of AIG, and dual China-Hong Kong listings for Agricultural Bank of China and two Chinese electrical-distribution firms.

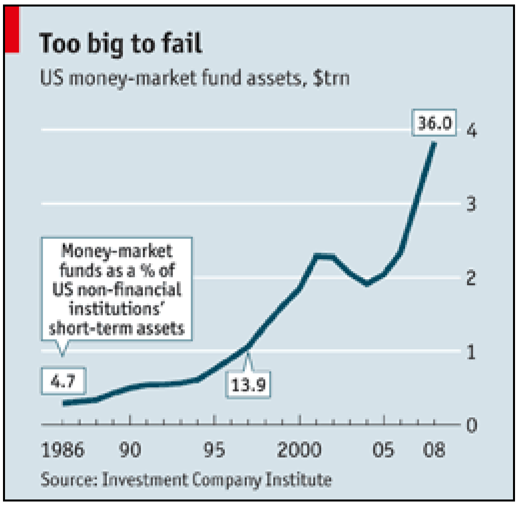
America's capital markets are benefiting too. Two Chinese companies, one producing specialty chemicals (Chemspec) and another water-treatment equipment (Duoyuan Global), made splashy debuts on the NYSE on June 23rd. In every case, regardless of where the listing venue might be, the underlying appeal is the same. Says Jonathan Penkin of Goldman Sachs in Hong Kong: “People are looking for growth. You can find it here.”

Money-market funds under scrutiny

Sleep therapy

Jun 25th 2009 | NEW YORK
From The Economist print edition

New rules designed to make money funds safer do not go far enough



BRUCE BENT, a money-market-fund pioneer, liked to say the industry should aim to bore you into a sound night's sleep. That was before it turned terrifyingly exciting, thanks largely to Mr Bent's own Reserve Primary Fund, which in September became the first money fund since 1994 to "break the buck", or fall below the $1 net-asset value per share that all funds seek to maintain. That triggered a run on money funds and traumatised the short-term debt markets they help to oil, forcing the American government to guarantee the industry's almost $4 trillion of assets—and confirming fears that it had become a big source of systemic risk (see chart).

With the guarantees due to expire in mid-September, pressure is on to tighten regulation. On June 24th the Securities and Exchange Commission (SEC) proposed a number of rule changes that are likely to go into effect after a brief comment period. Funds would be required to hold up to 10% of their assets in cash or bonds that can be sold within a day so they can more easily meet redemptions; to cut the maximum average maturity of their portfolios from 90 to 60 days to reduce interest-rate risk; and to buy only top-notch securities (up to 5% can currently be invested a grade below). Funds will also be allowed to suspend withdrawals if they break the buck, to allow for more orderly liquidation.

Welcome though these measures are, they fall short of the dramatic action needed to tame the systemic threat. The SEC deferred a decision (again) on whether to reduce overall reliance on credit ratings. It also postponed judgment on whether to eliminate the stable net-asset value, which would make money funds more like standard mutual funds, the prices of which fluctuate. Instead, this will be considered in a multi-agency report due in September.

Industry giants, such as Vanguard and BlackRock, have lobbied against moving to a floating asset value. It could prove counter-productive, sending investors scurrying to less regulated offshore vehicles that still offered a fixed price, argues Paul Schott Stevens, head of the Investment Company Institute, a trade group. The big question is whether money funds should be allowed to offer investors what amounts to a promise of capital preservation without having to succumb to bank-style supervision, capital requirements and insurance. Not for nothing are they called "shadow banks". A stable net-asset value may not be legally guaranteed, but shareholders treat it that way. As with banks, there is a mismatch (albeit a smaller one) between the term of funds' liabilities and their assets. And they will enjoy implicit government backing, in aggregate if not individually, once the temporary insurance ends.

Policymakers seem to have little stomach for treating money funds as banks, however, despite support for the idea from Paul Volcker, an adviser to Barack Obama. This suggests that they have been too quick to accept the industry's prediction that radical surgery would cause chaos; tellingly, Mr Stevens talks of a "meeting of the minds" with officials. As long as money funds are able to keep bank-like features without bank-like scrutiny, they should keep everyone wide awake.

Hedge-fund philanthropy

Alternative social investments

Jun 26th 2009 | LONDON AND NEW YORK
From The Economist print edition

Hedge-fund giving is proving surprisingly resilient

THIS has been the worst year or so in history for the hedge-fund industry, with many funds suffering deep losses and record numbers of them going out of business. Yet some leading hedge-funders remain firmly committed to giving away a chunk of their fortunes.

As *The Economist* went to press the Children's Investment Fund Foundation, a charity based in London, was due to announce that it had received a whopping £495m ($812m) in the 2008 fiscal year from TCI, a hedge fund, under covenants built into the fund when it was founded by Christopher Cooper-Hohn in 2003. The gift took the value of the endowment to just over £1.5 billion, all of which Mr Cooper-Hohn and his wife, Jamie, who oversees the day-to-day running of the foundation, will use to help children in the developing world.

Rex Features

Frugal Busson and bill-killer

Yet the crisis has taken its toll on London's hedge-fund philanthropists. In two instances, the Cooper-Hohns have filled (at least temporarily) a funding gap caused by partners suffering such deep losses that they could no longer fulfil their pledges to fund projects. On June 5th an annual gala and auction organised by Arpad Busson, a starry hedge-fund boss, for Absolute Return for Kids (ARK), another charity, raised £15.6m, well down from £25.5m in 2008.

That made the annual transatlantic hedge-fund give-off between ARK and the organisation that inspired it even less of a contest than usual. At its gala auction in New York in May the Robin Hood Foundation, which tackles poverty in the city, raised a record $72.6m, up from $56.5m in 2008 and topping by just over $1m the previous high in boom-era 2007. The achievement owed much to George Soros, the original hedge-fund philanthropist, who pledged to give up to $50m over two years if it was matched by a similar sum from Robin Hood's board members. That created a pool of up to $100m to be used to match other pledges.

In keeping with the times, both galas were lower-key affairs than usual. ARK cut the cost of the evening by two-thirds, and for entertainment attendees had to make do with a speech from Boris Johnson, the mayor of London. And Robin Hood's traditional auction of items such as dinner with Mikhail Gorbachev or a day on the set of the next James Bond movie, which has been criticised as a platform for rich show-offs, was replaced with a fund-raising session using wireless technology that allowed donors to give anonymously.

Friction in world trade

Duties call

Jun 25th 2009
From The Economist print edition

A row with China points to fraying tempers

DESPITE the periodic sighting of green shoots elsewhere in the economy, the landscape of global trade remains resolutely bare. The World Bank said on June 22nd that world-trade volumes, reeling from a drastic collapse in global demand (see chart), will shrink by nearly 10% this year. That would be the sharpest fall since the Depression, and the first decline in trade since a small dip in 1982.

Unsurprisingly, tempers are fraying as governments struggle to find ways to protect their own. The latest salvo was fired on June 23rd by America and the European Union, which complained to the World Trade Organisation (WTO) about China's restrictions on the exports of nine minerals, including bauxite, coke, magnesium and manganese. These are important raw materials for the steel industry, among others, and China restricts their exports on the grounds that they are exhaustible resources. But America and the EU argue that by hindering their export, China is unfairly favouring domestic industries.

John Veroneau, a former American deputy trade representative, believes the case against China is a strong one. He also argues that this week's move can be seen as an effort to foster more trade (as there surely would be if China were to ease its export restrictions) at a time when trade is in a great deal of trouble. In practice, it is unlikely to have that effect. If the case proceeds to the stage where a formal WTO panel is formed to decide on its merits, it could drag on for several years, by which time trade will, with luck, have recovered from its current moribund state.

Jeffrey Schott, a trade expert at the Peterson Institute for International Economics, a think-tank, says that the case against China may also help the cause of open trade in other ways. If Ron Kirk, America's new trade representative, demonstrates that he is actively enforcing the agreements already in place, he may get "the authority to negotiate Doha and other accords".

That may be too sanguine. True, America and the EU are not resorting to imposing fresh barriers of their own in this dispute; for that matter, China's export restrictions are not new either. But trade experts warn that protectionism remains a serious worry. Of particular concern are the so-called "Buy China" requirements added to China's stimulus package this month. These require recipients of money from China's mammoth fiscal expansion to choose domestic suppliers "unless products or services cannot be obtained in reasonable commercial conditions in China". This sounds like out-and-out protectionism. But America, which included similar "Buy America" provisions in its own stimulus bill, may find it hard to raise a stink.

The craze for clearing houses

Counter insurgency

Jun 25th 2009
From The Economist print edition

Central counterparties may not be all they are cracked up to be

CENTRAL counterparties (CCPs) have been part of the financial plumbing in exchange-traded markets since at least 1925, when the Board of Trade Clearing Corporation in Chicago took responsibility for settling grain futures. But they have never been so popular as now.

The idea is a good one. CCPs act as the buyer to every seller in a market, and the seller to every buyer. They collect margins on every trade; members put money into a reserve fund as well. Traders only have to worry about the creditworthiness of one entity, with which they can net off their trades. If a big trader goes under the financial system is less likely to go with it.

CCPs are the norm in exchange-based markets but they have been scarce among surging over-the-counter (OTC) derivatives, notably the gigantic market for credit-default swaps (see chart). OTC traders like to deal directly with each other, and their products are often too specialised to fit on an exchange. Reform is coming. America's Treasury called in May for all "standardised" OTC derivatives to be cleared through CCPs. The world's big banks have promised to clear more derivatives. On June 22nd a convention to standardise credit-default-swap (CDS) contracts for clearing took effect in Europe. New CCPs are sprouting everywhere.

Not everyone is happy about this trend. Craig Pirrong of the University of Houston worries that CCPs dull the incentive to trade prudently. Traders are more likely to take on risky positions because some of the losses they may generate are ultimately borne by others—the CCP and its other members. As for a CCP itself, however well intentioned it may be, it cannot monitor traders' complex derivative positions as well as they themselves can. And it is probably less motivated to try.

There is also a risk of creating too many CCPs. The scope for netting across all types of derivatives is reduced when CCPs are created to clear only one type of product; that could leave OTC traders with greater overall exposures than before. Even the benefit of netting within a single class of derivatives is impaired when more than one CCP starts up in the same market, which is precisely where things are heading. Three have been approved to clear CDSs in the past six months alone.

And while regulators fret that some banks are "too big to fail", they may be creating another set of institutions of equal systemic importance. "With their myriad clients the big trading banks in effect function as CCPs already," says Darrell Duffie of the Stanford Graduate School of Business. "Why double their number?"

CCP clearing may also impose greater demands on cash for businesses that currently use OTC derivatives. Whereas banks could tailor collateral requirements to the nature of their customers, CCPs will impose uniform margin requirements on everyone. If the benefits of CCPs in OTC markets are so overwhelming, why did they not emerge on their own?

Mortgage defaults in America

Can pay, won't pay

Jun 25th 2009
From The Economist print edition

It is easier to dump a home loan if a friend has done so too

HOUSE prices in America have fallen so far that as many as one in five households have mortgage debt greater than the value of their homes. In a few states, borrowers are not liable for the shortfall between an unpaid loan and the resale value of the home it is secured upon. Even where borrowers are on the hook, lenders often find it too costly to pursue unpaid debts. So some homeowners may be tempted to default and escape the burden of negative equity.

How widespread is this practice? New research* based on a survey of 1,000 homeowners suggests that one in four mortgage defaults are "strategic"—by people who could meet their payments but who choose not to. The main drivers of strategic default are the scale of negative equity, and moral and social considerations. Few would opt to renege on their mortgage if the equity gap were below 10% of their home's value, the authors find, partly because of the costs of moving. But one in six would bail out if loans were underwater by a half.

Four-fifths think strategic default is wrong. Those in the unethical minority are four times more likely to renege on loans (allowing for other influences) when their negative equity reaches $50,000. But morality has its price. When the equity gap reaches $100,000, "immoral" homeowners are only twice as keen to walk away from their debts as "moral" ones. People under 35 or over 65 are less likely to believe that default is wrong. So are the well-educated.

Anger about bail-outs of banks or carmakers does not weaken the moral barrier to default. But people who live in neighbourhoods where home repossessions are frequent are more likely to welsh on loans. Homeowners who know someone who has defaulted strategically are 82% more likely to say they would do so, too. The likelihood of strategic default rises more quickly once the rate of local home foreclosures reaches a critical level. That hints at a vicious cycle of foreclosures that both depress home prices and weaken the social and economic barriers to further defaults. To break the cycle, policymakers need to address the problem of negative equity, not just unaffordable interest payments.

* "Moral and Social Constraints to Strategic Default on Mortgages" by Luigi Guiso, Paola Sapienza and Luigi Zingales, University of Chicago Working Paper

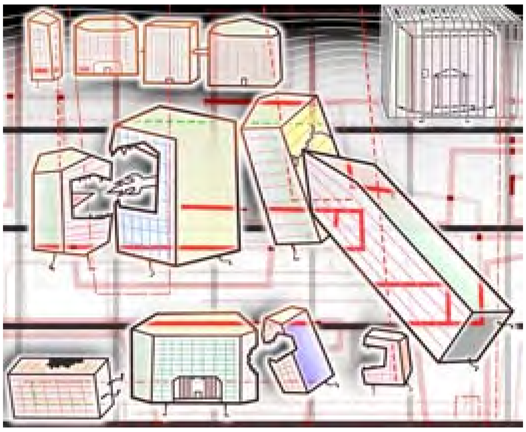
Economics focus

Deliver us from competition

Jun 25th 2009
From The Economist print edition

If competition in banking leads to too much risk-taking, the right remedy is better supervision

Illustration by Jac Depczyk



RICKY GERVAIS, a comedian, tells a story about an anxious flight. When informed that the airline no longer offered newspapers to passengers, in order to cut costs, he found it all too easy to imagine a maintenance worker inspecting the plane's undercarriage and asking: "Do we really need all these rivets?"

That firms which strive hard to sustain profits may act incautiously is a concern in many industries. The severity of today's financial crisis is blamed by some on the pressure of competition on banks. There is a bulky academic literature that links liberalisation of markets with an increase in bank failures. It argues that the lifting of restraints, such as interest-rate caps on deposits or rules that prevent banks from operating in certain markets, leads to more intense competition. That is good for borrowers, but it also hurts banks' profit margins by reducing the "franchise value" that comes from expected earnings.

A diminished franchise is not only bad for shareholders. By reducing the stake that banks have in their own long-term survival it may make bank failures more likely. A bank that could look forward to a stream of fat profits in a sheltered market would be careful to lend prudently to avoid a bankruptcy that would destroy the franchise. But a bank earning only lean and uncertain margins on garden-variety loans may have little to lose by gambling on riskier ventures. If these paid off, the bank would benefit. If they did not, depositors or government would pick up the bill.

This theory is backed by some empirical work. Research published in the *American Economic Review* in 1990 found that a measure of franchise values fell after restrictions were lifted on where banks could operate. Banks that lost market power as a consequence also held less capital as a buffer against bankruptcy. A more recent study by Vicente Salas, of the University of Zaragoza, and Jesús Saurina, director of the Bank of Spain's financial-stability wing, found the same pattern in Spanish banking. Fewer restrictions spurred competition, squeezed profit margins and led to more risk-taking by banks. (Not all the evidence points this way: though these studies of individual markets indicate that competition can lead to fragility, international comparisons suggest the opposite, according to a survey last year for the World Bank by Thorsten Beck, now of Tilburg University.)

There is clearly some tension between financial-stability goals and the tenets of competition policy, which hold that oligopolies are inefficient and serve consumers badly. Nevertheless, many policymakers seem to think that some curbs on competition may be a price worth paying to improve stability. Australia's banking system has come through the crisis intact, for example, and the former head of the country's central bank, Ian Macfarlane, has said that one reason for this is that the biggest four banks were banned from merging. Freed from the fear of a takeover, bank executives did not have to chase profits as aggressively as their brethren in America or Britain. This may explain why the big four banks have not needed a government bail-out and have retained high credit ratings. Another case where an unchanging market structure has gone hand in hand with financial stability is Canada. It still has the same five big banks it had two decades ago and none has needed to draw on state support.

Efficiency versus stability

The antitrust response is to say the problem is not too much competition but too little regulation. Trustbusters are rightly wary of special pleading on behalf of banking or other industries. A bank

bankruptcy may be troublesome if it triggers other failures and damages the whole payments and credit system. Yet there can be "systemic" problems in other competitive industries too. A food scare in one factory may prompt consumers to steer clear of similar products made by other firms, for example. But the remedy for worries about food safety is not to reduce competition but to regulate and enforce standards. So it should be in banking. Competition among airlines could in principle compromise passenger safety. That it does not is because of regulation. Setting Mr Gervais's worries aside, it is rarely suggested that food firms or airlines are less safe because of too much competition.

There is another reason not to treat banking as a special case. One route to market power is size. Consumers find it costly, or are often reluctant, to switch between banks so an industry dominated by a handful of firms is unlikely to be competitive. If the franchise-value argument is correct that ought, at least, to yield stability. What's more, bigger banks can diversify their earnings, which should further militate against failure. But a bank with sufficient market power would also be considered too big to fail, and would be rescued in the event of bankruptcy. Such knowledge can lead to excessive risk-taking and is one reason why Switzerland's central bank has said the country's two mega-banks may have to be cut down to size. Another idea in regulatory circles is to force big banks to hold a larger capital buffer than smaller ones.

For finance to be stable, banks have to bear the costs of their risk-taking. A bank's franchise value is one form of capital. It is lost forever if the bank fails and so is a guard against reckless gambling with deposits. The idea of bribing people to behave well (in this case, by letting banks enjoy market power) may be objectionable but is at least familiar. The theory of "efficiency wages" says that firms which cannot monitor workers' efforts well should instead pay high wages to make it costlier for them to risk being sacked. But it would be far better to keep a closer eye on banks and force them to match their tangible capital with their risk-taking appetite. By making banks build reserves in good times and reducing their room to get around capital regimes, Spain's regulators drew the right lesson. Where competition leads to more risk-taking, the correct response is to monitor banks more closely.

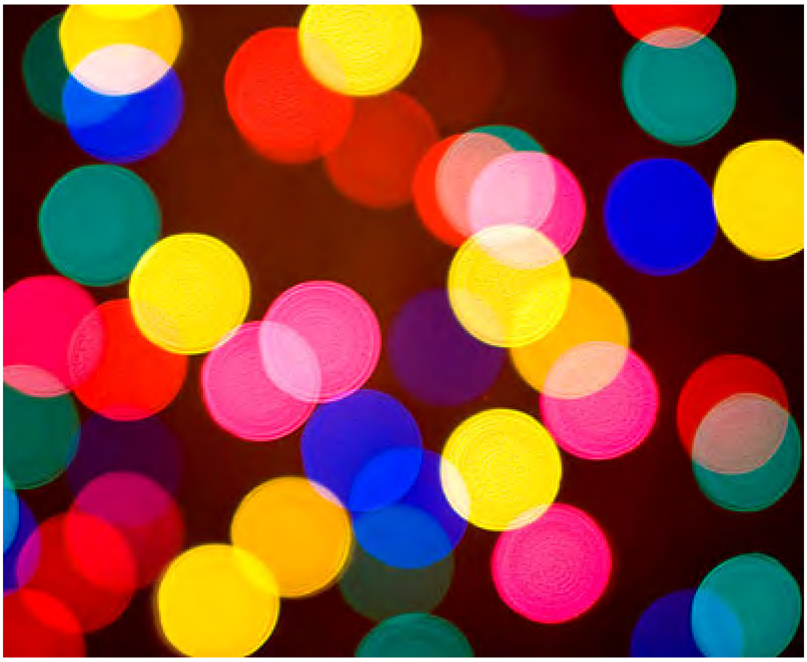
A new display technology

Spots of innovation

Jun 25th 2009
From The Economist print edition

Magnetic microspheres could have a range of colourful applications

Alamy



A FEW years ago Yadong Yin was experimenting with tiny beads that changed colour when a magnetic field was applied to them. This was interesting but, as the beads floated around in water with no obvious way to turn them into a product, people asked: What could be done with them? Now Dr Yin and his colleagues at the University of California, Riverside, have carried out more experiments and have come up with possible applications that range from a new type of paint to lipsticks and giant advertising billboards.

Dr Yin's beads are magnetochromatic microspheres. They are made from tiny blobs of polymer that contain particles of iron oxide. The structure of these particles changes in a magnetic field in a way that produces "interference" colours when light is shone on them. Interference, in which fine details on an object's surface cause light waves to cancel each other in some places and reinforce one another in others, is what creates the iridescent colours of many bird feathers, butterfly wings and beetle shells. In the case of Dr Yin's beads, it is the rearrangement of the particles' microstructures that produces the pertinent detail.

To make their spheres Dr Yin and his colleagues stir iron-oxide particles into a liquid polymer resin, which is then dispersed in oil. The oil and the resin will not mix, so the result is droplets of resin floating in the oil. A magnetic field is then applied to the droplets to produce the required colour and the colour is fixed by curing the polymer into a solid structure.

The kingfisher's wing

Or, rather, it is almost fixed. For, just as the colour of an iridescent feather changes with the angle you look at it, so the colour of a droplet can be changed by rotating it. It can even be switched on and off. Moreover, since the form of iron oxide used to make the droplets is magnetic, a magnetic field can be used to rotate them. And, by rotating groups of microspheres of different colours in this way it should be possible—if they are suitably arranged—to create images, including moving ones.

The spheres have to be dispersed in some form of liquid medium if they are to rotate. But, as Dr Yin observes, that medium does not have to be liquid all the time. It could, for example, be a wax. When the wax was heated, the spheres would be able to change orientation, but they would be held in place when it cooled and solidified again.

The researchers, whose latest study is published in the *Journal of the American Chemical Society*, say there are a number of ways their spheres could be employed. Because they can be tuned across the whole spectrum they might provide a safe and environmentally friendly replacement for pigments in paint. Iron oxide, after all, is not toxic. They could also be used in other coloured substances, such as ink, cosmetics and textiles.

In theory, the moving version of the product might be used in computer and television screens. In practice, Dr Yin thinks liquid-crystal technology is so well developed that his microspheres will never catch up. But they could form pixel-like elements in posters and outdoor signs, allowing those signs to be updated, or even to display videos. Such signs would not have to be backlit in the way that a screen is, and they would probably be cheaper to make than liquid-crystal displays.

Dr Yin, a chemist, is collaborating with a team at Seoul National University in South Korea to produce a control system to switch the colour of microspheres on display devices so that they can form moving images. One way this might be done is to place a grid of wires behind them and induce a magnetic field where the wires cross. The spheres at the intersections would then rotate. But the speed of change may be less important in an otherwise static image on an outdoor billboard than it is on a television, so a scanning process that moved in increments across rows of microspheres would probably be just as effective. It might take a little time, but it would be more convenient than climbing up a ladder with a big bucket and a brush to paste on new sheets of paper.

The earliest granaries

Food for thought

Jun 25th 2009
From The Economist print edition

Storing grain predates agriculture, and may have propelled it

THE period when humans stopped hunting and gathering and settled down to become farmers is one of the most important in history. It ranks with the original human exodus from Africa about 60,000 years ago, which led to *Homo sapiens* becoming a global species, and the beginning of the industrial revolution, 250 years ago, when many people stopped being farmers and began to earn their livings in other ways. Yet it is not well understood. A piece of research published this week in the *Proceedings of the National Academy of Sciences* by Ian Kuijt of the University of Notre Dame, in Indiana, and Bill Finlayson of the Council for British Research in the Levant, may shed more light on the matter.

Dr Kuijt and Dr Finlayson have been excavating a site called Dhra, in Jordan, near the Dead Sea. They have uncovered evidence that sophisticated ways of storing grain had been developed well before cereals were actually domesticated. The discoveries the two researchers describe appear to be small granaries, about three metres across and three high. They are made of mud, in some cases reinforced by stone. But, being over 11,000 years old, they predate the domestication of cereals in the Middle East by a millennium. Instead, they seem to have been used to store wild barley and wild oats.

The period leading up to the domestication of cereals was one of erratic climate change, as the last ice age ended. In the Middle East people started to build settlements as early as 15,000 years ago, a period called the Early Natufian, but a drying of the climate made them nomadic again between 12,800 and 11,500 years ago. A second attempt to settle, known to archaeologists as the Pre-Pottery Neolithic A, then began and led, arguably, to modernity—at least in the West.

The granaries themselves are circular and quite sophisticated. From the arrangement of a system of internal stone supports, for example, they appear to have had raised floors. That would have allowed air to circulate, reducing the risk of fungal spoilage and providing some protection against rodents. The floors also sloped, apparently deliberately—probably to make moving grain around them easier. And evidence of barley straw at the site helps confirm that the buildings were, indeed, used to store grain.

To settle down in one place requires a reliable food supply, so the discovery of granaries is no surprise. Pits that might (or might not) have held grain have already been found, but the latest discovery is on a far grander scale. It helps confirm what had previously been suspected—that it was a technological change to the gathering half of the hunting-and-gathering lifestyle that propelled the domestication and cultivation of crops.

What happened next (indeed, what was probably already happening) was the deliberate planting of wild seeds, in order to make the gathering process less onerous. From there, it was but a short leap to choosing seeds from the most productive plants to sow next season and the consequent evolution, partly by accident and partly by design, of early versions of many of the grains that now feed the world.

Informed consent and virtual worlds

The avatar will see you now

Jun 25th 2009
From The Economist print edition

A way of helping the mentally impaired to give informed medical consent

Imperial College

Virtually painless

THAT people undergoing medical procedures should give their informed consent might seem simple and uncontentious. But what if a patient has a mental impairment and his doctor does not have time to ensure he understands the proposed treatment? Those who try to look after the interests of such people say that, in practice, hard-pressed hospital staff often ask leading questions and the "consent" obtained is thus far from informed.

A team of researchers led by Suzanne Conboy-Hill, a psychologist at the Royal Sussex County Hospital in Brighton, England, reckon virtual environments could provide the solution. They are designing a virtual model of the hospital and, in October, it will receive its first "patients"—a group of 20 volunteers with learning disabilities who will visit it in order to find out what's what and, in particular, to be talked through the sort of treatment they might be offered if they really were patients.

The hospital is being built in Second Life, an online world in which people participate in the form of virtual representatives known as avatars. In the case of those in the study, their digital alter egos will begin their journeys at a simulation of the Grace Eyre Foundation centre for adults with learning disabilities in Brighton, which they attend in real life. Local landmarks such as the town's famous seaside pier will be used to help familiarise them with their surroundings before they arrive at a virtual version of the Royal Sussex.

This particular version of Brighton will, however, be based in London. It will be hosted in a private part of Imperial College's virtual postgraduate medical school in SciLands, a dedicated science and technology Second Life continent populated by around 30 universities, government agencies and museums. Once inside the hospital, the avatars will be directed to a waiting room. Then a virtual nurse will take them to a bed, where they will lie down to have virtual blood taken. A Second Life doctor will explain that they are about to have an anaesthetic. Meanwhile, a real person alongside the participant will answer any questions and, after the virtual visit is over, Dr Conboy-Hill will carry out "non-directive" interviews, a technique used by the police to encourage witnesses to choose what they want to talk about and to maximise recall.

If these interviews suggest the participants understood what was going on well enough to give informed consent, then the researchers plan to carry out a larger study, comparing their simulation directly with the standard method of obtaining consent face to face. If it proves better, who knows, it might not only be the mentally impaired who find that virtual doctors are better at explaining things than real ones.

Lightweight dinosaurs

Not so terrible

Jun 24th 2009
From The Economist print edition

Prehistoric monsters may not have been as monstrous as once believed

The Art Archive

Svelte!

DINOSAURS—terrible lizards, to translate their name into English—were big. Of course, there were many small ones, too. But what caught the public imagination in the 19th century, when the first of them were dug up, and has not let go of it since, is the idea that some dinosaurs were unfeasibly huge; the largest animals, by a long chalk, ever to walk the face of the Earth.

Gary Packard of Colorado State University and his colleagues do not deny that creatures like *Apatosaurus*, *Brachiosaurus* and *Diplodocus* were big—and bigger than any terrestrial mammal. But they do question just how big. In a study published this week in the *Journal of Zoology*, they examine the method traditionally used to estimate the weight of extinct animals from their fossilised bones and find it wanting. Their revised version has slimmed some of the giants by 50%.

A specimen of *Apatosaurus* (better known to many laymen as *Brontosaurus*) that had been examined using the previous method is now thought to have weighed 18 tonnes rather than 38 tonnes—the equivalent of only about three fully grown African elephants, instead of seven. A *Brachiosaurus* slimmed down from 32 tonnes to 16. Even a slender *Diplodocus*, once believed to have tipped the scales at five and a half tonnes when alive, has lost a tonne and a half from its weight.

Working out an animal's mass from the size of its bones is not, of course, an exact science. But it is possible to use the weights and bone sizes of existing species to make mathematical models of the relationship. The problem comes when these models are used to extrapolate beyond the range of reliable data (ie, of living animals whose weight is known). Since the largest dinosaurs have skeletons a lot larger than any living terrestrial species, such extrapolation is fraught with difficulty.

Dr Packard and his colleagues argue that the most widely used model has got the extrapolation wrong. It uses what are known as logarithmic transformations to cope with changes in the relationship between bone size and weight. This works well enough for smaller animals, but it predicts that an elephant should weigh one and a half times as much as it actually does, and that deviation is likely to be much larger for a *Brachiosaurus*, *Apatosaurus* or *Diplodocus*.

Dr Packard's model gets round this by abandoning simple logarithmic transformation in favour of a more complicated, so-called nonlinear model. This fits the data for existing large species better and so, he concludes, may provide a better estimate of the weights of large extinct ones.

Of course, no one can know for sure. Despite the confident depiction of them in films such as "Jurassic Park", the reconstruction of dinosaurs is subject to constant re-interpretation. But even at a mere 18 tonnes, *Apatosaurus* would still have been an awesome sight.

The evolutionary origin of depression

Mild and bitter

Jun 25th 2009
From The Economist print edition

Depression may be linked to how willing someone is to give up his goals

CLINICAL depression is a serious ailment, but almost everyone gets mildly depressed from time to time. Randolph Nesse, a psychologist and researcher in evolutionary medicine at the University of Michigan, likens the relationship between mild and clinical depression to the one between normal and chronic pain. He sees both pain and low mood as warning mechanisms and thinks that, just as understanding chronic pain means first understanding normal pain, so understanding clinical depression means understanding mild depression.

Dr Nesse's hypothesis is that, as pain stops you doing damaging physical things, so low mood stops you doing damaging mental ones—in particular, pursuing unreachable goals. Pursuing such goals is a waste of energy and resources. Therefore, he argues, there is likely to be an evolved mechanism that identifies certain goals as unattainable and inhibits their pursuit—and he believes that low mood is at least part of that mechanism.

It is a neat hypothesis, but is it true? A study published in this month's issue of the *Journal of Personality and Social Psychology* suggests it might be. Carsten Wrosch from Concordia University in Montreal and Gregory Miller of the University of British Columbia studied depression in teenage girls. They measured the "goal adjustment capacities" of 97 girls aged 15-19 over the course of 19 months. They asked the participants questions about their ability to disengage from unattainable goals and to re-engage with new goals. They also asked about a range of symptoms associated with depression, and tracked how these changed over the course of the study.

Their conclusion was that those who experienced mild depressive symptoms could, indeed, disengage more easily from unreachable goals. That supports Dr Nesse's hypothesis. But the new study also found a remarkable corollary: those women who could disengage from the unattainable proved less likely to suffer more serious depression in the long run.

Mild depressive symptoms can therefore be seen as a natural part of dealing with failure in young adulthood. They set in when a goal is identified as unreachable and lead to a decline in motivation. In this period of low motivation, energy is saved and new goals can be found. If this mechanism does not function properly, though, severe depression can be the consequence.

The importance of giving up inappropriate goals has already been demonstrated by Dr Wrosch. Two years ago he and his colleagues published a study in which they showed that those teenagers who were better at doing so had a lower concentration of C-reactive protein, a substance made in response to inflammation and associated with an elevated risk of diabetes and cardiovascular disease. Dr Wrosch thus concludes that it is healthy to give up overly ambitious goals. Persistence, though necessary for success and considered a virtue by many, can also have a negative impact on health.

Dr Nesse believes that persistence is a reason for the exceptional level of clinical depression in America—the country that has the highest depression rate in the world. "Persistence is part of the American way of life," he says. "People here are often driven to pursue overly ambitious goals, which then can lead to depression." He admits that this is still an unproven hypothesis, but it is one worth considering. Depression may turn out to be an inevitable price of living in a dynamic society.

Milestones

Jun 25th 2009 | ATHENS
From The Economist print edition

A new tribute to the Parthenon

Reuters

AS GREECE'S first Socialist culture minister in 1981, the late Melina Mercouri, a flamboyant actress best known for playing a golden-hearted prostitute in a film called "Never on Sunday", decided to make her mark in politics by campaigning for the return of the Elgin marbles from the British Museum (BM) (see article).

Mercouri's pleas to officials in London were ignored, but she scored two successes. First, the fifth-century-BC sculptures that Lord Elgin, a British diplomat, removed from the Acropolis temples in 1801-05 and later sold to the BM have become more widely known as the Parthenon marbles—the name chosen by Mercouri to highlight where they came from. More important, her campaign added fuel to an international debate over who owns cultural property, whether ancient Greek or ethnic African, that has burned ever since.

On June 21st a new museum opened in Athens to display the Parthenon sculptures and other finds from the Acropolis hill, fulfilling Mercouri's promise that Greece would one day build a suitable home for the Parthenon frieze and other exiled masterpieces of classical art. At the opening ceremony—attended by José Manuel Barroso, president of the European Commission, and Koichiro Matsuura, director-general of UNESCO, the UN agency for cultural heritage—Antonis Samaras, the current Greek culture minister, made a point of condemning the 19th-century "looting" of treasures from the Acropolis. Also present were representatives of committees in 17 countries that campaign for the marbles' return, as well as the deputy chairman of the BM's board of trustees.

The €130m ($180.5m) new Acropolis Museum, a stack of glass-and-concrete boxes designed by Bernard Tschumi, a Swiss-born architect based in New York, together with Michael Photiadis, his Greek associate, is uncompromisingly modern. Its glittering bulk, squeezed into a narrow plot beneath the Acropolis hill, contrasts sharply with shabby blocks of flats nearby and the pale-coloured rocky slope. Some Athenians complain it is simply too big for the site. Yet both Greek and foreign visitors seem delighted by the museum's spacious, daylight-filled interior.

In the first-floor gallery, free-standing marble statues of men, women and horses glow against a background of grey concrete walls and columns. Floor-to-ceiling windows are made of thick crystalline glass embedded with mineral particles to cut out glare. Mr Tschumi says, “The marble reflects light, but the concrete absorbs it…the use of daylight is fundamental to this museum.”

Glass floor-panels in connecting spaces illuminate an excavation in the basement of the museum (soon to be opened to visitors) of houses and streets in an Athens neighbourhood dating from early Christian times.

The caryatids, five larger-than-life-size female statues that supported a porch on the Erechtheum temple on the Acropolis, survey the museum’s lobby from an internal balcony. An empty space has been left for the sixth, which is in London.

Mr Tschumi’s showpiece is the top-floor Parthenon gallery, a cool glass box with a spectacular view that mirrors the dimensions and orientation of the temple itself. Below, projected on the wall, is a digitised video animation of elegant *korai* statues (pictured above).

The frieze, a mix of honey-coloured marble panels and glaring white plaster casts of pieces in the BM, shows a procession of worshippers carrying offerings to Athena, the temple goddess. It is mounted at eye level on a grey concrete wall, an arresting display that could almost be an installation in a contemporary art show.

Dimitrios Pandermalis, the museum’s director, says, “We thought about leaving gaps for pieces that are in London, but we eventually decided that the casts would give continuity while making it quite clear how the frieze has been divided.”

By comparison with Athens, the BM’s display, which amounts to half the remaining frieze, and which was improved in 1998, now looks a little tired. Alexandros Mantis, a Greek expert on the ancient Acropolis temples, also points out that the frieze, which ran around the exterior of the Parthenon, is arranged in London around the interior of a gallery, which is architecturally and aesthetically wrong.

For the Greeks, criticised in the past for not having a suitable place to display the Acropolis sculptures, the inauguration of the new museum is the strongest possible argument for repatriating the marbles.

Moreover, it fulfils a widespread belief that architectural sculpture should be displayed as close as possible to the building it once decorated. Atmospheric pollution rules out placing the sculptures back on the temple itself. But the Parthenon gallery in the new museum is 300 metres and a single glance away from the temple.

However, Neil MacGregor, the BM director, is as passionate (and as eloquent) about keeping the marbles in London as the Greeks are about getting them back. Mr MacGregor argues that they have belonged to a unique collection for more than 200 years, in a museum that attracts more visitors than any other in the world, rather than just to one nation’s history.

An eventual solution—though probably not one that will happen on Mr MacGregor’s watch—would be to send the marbles back to Athens on loan and accept the Greek offer to provide a series of temporary exhibitions of classical art to fill the gallery. But that would require the Greeks to recognise British ownership of the sculptures in London, something Mr Samaras says would be “impossible”.

With mutual prickliness running high, the stand-off looks set to continue. In the meantime, though, Athenians and their visitors can be proud of their stunning new piece of architecture, filled with indisputably great art.

Books on the credit crunch

First draft of history

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The search is on for the ideal book about the financial crisis

Reuters

Chasing Alpha: How Reckless Growth and Unchecked Ambition Ruined the City's Golden Decade. By Philip Augar. *The Bodley Head; 259 pages; £20.* Buy at Amazon.co.uk

Fool's Gold: How the Bold Dream of a Small Tribe at J.P. Morgan Was Corrupted by Wall Street Greed and Unleashed a Catastrophe. By Gillian Tett. *Free Press; 304 pages; $26. Little Brown; £18.99.* Buy at Amazon.com, Amazon.co.uk

Lecturing Birds on Flying: Can Mathematical Theories Destroy the Financial Markets? By Pablo Triana. *John Wiley; 400 pages; $29.95 and £19.99.* Buy at Amazon.com, Amazon.co.uk

The Spectre at the Feast: Capitalist Crisis and the Politics of Recession. By Andrew Gamble. *Palgrave Macmillan; 184 pages; $26.95 and £14.99.* Buy at Amazon.com, Amazon.co.uk

Restoring Financial Stability: How to Repair a Failed System. Edited by Viral V. Acharya and Matthew Richardson. *John Wiley; 401 pages; $49.95 and £33.99.* Buy at Amazon.com, Amazon.co.uk

THE credit crunch may have caused a bust in the economy but it has created a boom in financial publishing. It seems as if every journalist or academic who ever entered a bank has rushed to bring his or her opinions into print. They have taken on a Herculean task.

The best financial books—"Barbarians at the Gate" or "The Smartest Guys in the Room"—have been built around specific deals or companies (the takeover of RJR Nabisco, the collapse of Enron). The credit crunch has been much more diffuse, involving macroeconomic imbalances, greedy and incompetent bankers and fraudulent American homebuyers. Try covering the lot and the book can seem rambling and shapeless; narrow your focus and you miss the broader picture.

The ideal book on the crisis would not only tell readers what happened during the crunch and why. It would also look ahead at how the system will change. And it would be accessible, even to readers who have not spent years studying the minutiae of the financial markets.

Philip Augar's "Chasing Alpha" scores well on both historical explanation and readability. In a sense this book is a follow-up to "The Death of Gentlemanly Capitalism" (2000), in which he dissected the takeover of the British financial sector by Americans and Europeans. "Chasing Alpha", again with a largely British bent, explains how the interplay between banks and investors ended up in an orgy of risk-taking. The analysis is excellent. It is a shame, however, that Mr Augar is let down by sloppy fact-checking. For example, Alan Greenspan's "irrational exuberance" speech was given in 1996, not 2000. This is not the only error.

Gillian Tett's "Fools Gold" is more narrowly focused on the world of credit derivatives, the alphabet soup of CDOs and SIVs that were at the heart of the crisis. The action is seen through the prism of the derivatives team at JPMorgan, which helped create the toxic products. While Ms Tett's explanation of the technicalities is first class, the fact that JPMorgan survived the crisis better than most robs the book of some drama. One longs instead to have a similar inside view from Bear Stearns, Lehman Brothers and Merrill Lynch, the investment banks laid low by their exposure to dodgy American housing loans.

The alternative to the structure adopted by Mr Augar and Ms Tett is to take a thematic approach. Pablo Triana's "Lecturing Birds on Flying" laments the way that mathematicians and financial economists have

appeared to take over the markets. Economics is not a science like physics because humans are forever adapting their behaviour in the light of others' actions. The models devised by the maths gurus were not just unlikely to work, he argues, they also gave bankers a false sense of security, leading them to take more risks.

Mr Triana compares one widely used system, the value at risk (VAR) measure, to a passenger airbag that works 95% of the time; unfortunately the other 5% includes the time when the driver has an accident. Rather than rely on models which can never capture the complexity of human interaction, banks and investors should instead trust the judgment of experienced traders and managers.

The book is fizzing with ideas but the reader has to wade through Mr Triana's verbose and convoluted prose, of which the final sentence is surely the most depressing example. "Deliciously paradoxically, the Nobel could end up diminishing, not fortifying, the qualifications-blindness and self-enslavement to equations-led dictums that, fifth-columnist style, pave the path for our sacrifice at the altar of misplaced concreteness."

Arguably, all this focus on derivatives and risk models ultimately misses the point. In the end, this financial catastrophe has been like every other; banks lent too much money during a property boom and now (together with the unfortunate taxpayers) they are paying the penalty. Andrew Gamble's "The Spectre at the Feast" sees the downturn as the latest in a series of capitalist crises. And he uses the word crisis, not in the short-term sense of a tabloid headline, but as an historical turning point when the economic system is remade, just as the Great Depression led to the adoption of social safety nets.

Mr Gamble, professor of politics at Cambridge University, offers a brisk tour of economic history over the past 30 years, and argues that the financial sector was the chief beneficiary of the "neoliberal" policies introduced by Ronald Reagan and Margaret Thatcher. The fact that governments have had to nationalise, or prop up, many of the leading banks suggests that a rethink is in order. Unfortunately, the author does not produce any startling insight on what that rethink might involve.

Of this pile, the book that best combines history, analysis and prescription is "Restoring Financial Stability", a series of essays by academics at New York University's Stern School of Business. The 60-page prologue is packed with telling facts and sophisticated analysis, and alone is worth the steep cover price. The individual chapters deal methodically with the myriad issues raised by the crunch, and the policy changes that will be needed, covering everything from the American mortgage market to the need for international co-operation in regulating finance.

The Stern book may be careful to avoid academic gobbledygook and complex equations, but it cannot be described as a light read. That suggests it will not turn out to be the defining tome on this crisis. Producing that book may require a little more perspective. It is worth remembering that J.K. Galbraith's masterly work, "The Great Crash, 1929", was not published until a quarter-century after the event.

Violence in eastern Anatolia

Give up the g-word

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From The Economist print edition

Illustration by Daniel Pudles

Rebel Land: Among Turkey's Forgotten Peoples. *By Christopher de Bellaigue.* Bloomsbury; 288 pages; £20. Buy from Amazon.co.uk

MOST of the people who devote themselves to chronicling the history of Anatolia during the first world war fall into one category or another: those determined to prove that the Armenians suffered genocide, and those determined to prove the opposite. This Manichean split amounts to a "travesty of history and memory". What is needed is a "vaguer designation, avoiding the g-word but clearly connoting criminal acts of slaughter."

That is Christopher de Bellaigue's argument and many people will be shocked by it. How could anyone want to blur the outlines of an unspeakable phenomenon whose precise definition has, in recent years, been of keen concern to liberal internationalists and humanitarian law buffs? What hope is there of stopping genocide if people do not even try to decide what the word means?

But honest readers of this moving and intricately woven look at Turkey's 20th-century history will surely see his point. By focusing on a single, remote area in the east Anatolian highlands, and describing not only its blood-drenched history but the multiple layers of denial that obscure every episode, Mr de Bellaigue, a former correspondent for this newspaper, conveys some important messages about the elusiveness of historical truth.

As he shows, in places where "the past is not even past", the passage of time does not always make it easier to discern or speak the truth. It is difficult, though not impossible, to establish even the basic facts about the fate of the Armenians in this part of Anatolia; it is also hard to establish what horrors occurred during the Kurdish uprising which began in the 1990s and is still sputtering away.

So many of the people who might be able to offer enlightenment—be they local residents, or migrants to Istanbul or Germany—are consciously or unconsciously hiding truths: about themselves and their family histories, as well as more public events. For example, some Armenians who escaped in 1915 were re-socialised as Turks or Kurds, without entirely losing their genetic memory. This has odd effects on the way such people, and their descendants, think and talk; this book analyses those effects shrewdly but not unkindly.

Indeed, the best thing about the book is the intelligence with which the author deconstructs all the private and public myths that seem to be haunting his interlocutors, including the various servants of the Turkish state who take it upon themselves to set him straight about their country's history.

Many of his official informants assume that a person of Anglo-Saxon appearance, speaking fluent Turkish,

must belong to the long line of spies and troublemakers who have meddled in this part of the world on behalf of perfidious Albion. The reader is not invited to mock or despise these envoys of the state. On the contrary, the feeling is that for all the peculiar and indeed downright wrong things they believe, such people have their own particular integrity.

As an account of the way truth is constructed by communities and families living in a state of war and fear, “Rebel Land” ranks in sophistication with any primer of postmodern philosophy or social anthropology. It is also far more gripping, not least because it is told in the vulnerable but never self-indulgent voice of somebody who loves this part of Turkey, and has a soft spot for all the peoples who have lived, loved, died and killed there.

Constitutional democracy

Power to the people

Jun 25th 2009
From The Economist print edition

The New British Constitution. By Vernon Bogdanor. *Hart Publishing; 392 pages; £17.95.* Buy from Amazon.co.uk

Democracy: 1,000 Years in Pursuit of British Liberty. By Peter Kellner. *Mainstream Publishing; 540 pages; £25.* Buy from Amazon.co.uk

"THE British Constitution has always been puzzling and always will be," Queen Elizabeth II was once overheard saying. Until recently it was a puzzle that 99% of Britons would happily have left unsolved. But public disenchantment with established politics was growing even before this year's scandal over MPs' expenses replaced apathy with scorn. Now, as politicians try to wheedle their way back to respectability, all sorts of constitutional changes are suddenly on the table, distracting just a touch from the more painful task of punishing the fiddlers and tightening the rules. Boot out the unelected peers forthwith! Replace first-past-the-post voting for Westminster seats with proportional representation! And how about that old favourite, a written constitution?

Britain does have a written constitution, of course, but it is not written all in one place, with a catchy preamble to make clear its basic principles. Lacking a "constitutional moment"—a sharp and unreversed break in its history—Britain saw its constitution evolve through centuries of accumulated legislation and conventions.

For the constitutional theorists of Victorian times (among them Walter Bagehot, late of this newspaper), the guiding principle was simple: Parliament was sovereign (though, after the rise of party politics in the 19th century, the executive drawn from it called the shots) and its laws were unchallengeable throughout the land. The constitution was not a set of fundamental and broadly unalterable rules but simply "what happened". The fact that government's workings could easily and unobtrusively be changed was accounted a virtue: Britain escaped the ancestor worship that fixed canons like America's imposed. Its elusive constitution seemed to ensure both stability and freedom. It was envied abroad and taken for granted at home.

That domestic consensus, like so much in Britain, began to wear thin after the second world war. The title of Vernon Bogdanor's latest book on constitutional matters suggests the rest. Lurchingly, Britain is becoming a country in which central-government power is limited in different ways. Joining the European Economic Community in 1973 began to push power up to Brussels. Incorporating the European Convention on Human Rights into domestic law in the Human Rights Act pushed power sideways, to judges who are required to assess whether laws violate its provisions. Devolving power to Scotland, especially, pushed it downward.

These and other changes have produced—piecemeal, incomplete and largely unnoticed—a new British constitution. Parliamentary sovereignty is being replaced with a body of fundamental laws and greater separation between the executive, the legislature and judiciary, aka constitutional sovereignty. But these reforms have not rejuvenated British politics, Mr Bogdanor maintains, because they have redistributed power among elites, rather than between elites and the people. Though deference has long since died and an increasing proportion of Britons boast a university education, participation in formal politics, as in many other countries, is declining. Britain is becoming a constitutional state, but not a popular one.

The next step in Britain's unheralded revolution, therefore, is giving more power to the people. Mr Bogdanor, an Oxford don and long a toiler in the constitutional vineyard, is a man with a mission. He is a fan of proportional representation, and this figures among his proposals for change, along with primaries to select parliamentary candidates, greater use of referendums and citizens' assemblies to make laws on important issues. And should the constitution in fact be codified? His position is impressively Augustinian, if a bit limp: there are "powerful intellectual arguments" for it, but not yet.

This is a beautifully written book, the language as clear as the thinking, and it could not be more timely. Another, quite different offering complements it: Peter Kellner's new compendium of texts on British democracy from Athelstan the Glorious to Gordon Brown the Inglorious.

In the course of it the reader is reminded that as the "Mother of Parliaments" Britain was far from first in the field (Iceland's Althing met much earlier), and that *habeas corpus*, that cornerstone of British liberty, passed on to the statute book in 1679 through a deliberate miscount in the House of Lords, Mr Kellner has explained. Lord Norris, the teller for the bill's supporters, counted the "inordinately fat" Lord Grey as ten votes rather than one. The author's often hilarious commentary fails utterly to disguise his passionate reverence for Britain's democratic heritage.

Werner Herzog and "Fitzcarraldo"

Drama and melodrama

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From The Economist print edition

Conquest of the Useless: Reflections from the Making of Fitzcarraldo. By Werner Herzog. *Ecco; 320 pages; $24.99 and £14.99.* Buy it from Amazon.com, Amazon.co.uk

Kobal Collection

Compelled by Caruso

WERNER HERZOG'S 1982 film, "Fitzcarraldo", was inspired by a would-be rubber baron who hauled a boat over a Peruvian mountain to harvest an inaccessible forest of rubber trees because he wanted to build an opera house in the jungle. Fired by the image of "a large boat scaling a hill under its own steam" while the voice of Enrico Caruso soars above the landscape, Mr Herzog insisted, when he came to make the film, on duplicating the exploit with a real steamship, only on a steeper gradient. And when, halfway through shooting, the actor playing Fitzcarraldo had to leave the set, Mr Herzog started from scratch, this time directing his old friend and enemy, Klaus Kinski, in the role—an extreme sport if there ever was one.

The film the two of them made is a sweet, funny ode to eccentricity that is nothing like their first collaboration in the Peruvian jungle, the nightmarish "Aguirre, the Wrath of God" (1972). That sweetness comes through in "Conquest of the Useless", Mr Herzog's memoir of making "Fitzcarraldo", when the director's good nature never fails him, even during an eyeball-to-eyeball encounter with a boa constrictor. "Stubbornly confronting each other, we were pondering the relatedness of the species. Both of us, since the relatedness was slight, felt sad and turned away from each other."

These moments, when the film-maker looks into the eyes of lizards or a bad-tempered albino turkey, set the tone for his relations with all of creation, including his crew, to whom he is unfailingly kind. A gifted writer, Mr Herzog alternates poetic prose descriptions with accounts of his fevered dreams, though the distinction between the two is not always clear. He also has a sharp eye for grotesque detail: "At the market I ate a piece of grilled monkey," he writes at the outset of his journey. "It looked like a naked child."

Initially shocking, these sights serve to inspire some of the more enigmatic metaphors of the film. After an episode in which an umbrella is blown out of his hand by the wind, only to land in the river with the handle sticking up, the director writes it into the film, where it appears as a relic of a murdered missionary sent as a warning to the expedition by the fierce Jivaro Indians. Fitzcarraldo responds by bombarding the invisible enemy with yet more Caruso.

Opera, Mr Herzog argues, makes the most outlandish events beautiful by transforming the world into music and reducing it to its bare emotional essentials. "That's what opera and the jungle have in common," he concludes; a metaphor that sums up the craziness of Mr Herzog's epic film and his memoir about making it.

Correction: “Phèdre”

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In our article about the National Theatre’s production of “Phèdre” (“Serried ranks”, June 20th), we stated that Racine wrote the play in iambic pentameters. The meter was, of course, alexandrines. This has been corrected online.

Ralf Dahrendorf

Jun 25th 2009
From The Economist print edition

Ralf, Baron Dahrendorf, thinker and politician, died on June 17th, aged 80

AP

AS A man who spent his life defining and defending liberty, Ralf Dahrendorf treasured the moment when he first felt that "visceral desire not to be hemmed in". He was in prison and in solitary, sent there for being part of a schoolboys' anti-Hitler society. He was not yet 16. Determined to demonstrate his free spirit somehow, he tore a piece of brown paper out of his mattress and wrote down, with a blunt pencil he had cadged from a guard, all the Latin words he could remember. In the preservation of liberty, he wrote later, "We have the weapons we need, our minds".

The advancing Red army eventually freed both him and Germany. For a while, there was neither government nor rules. With a band of young friends, he looted the local shops in Berlin. Through his long and stellar academic career, on his professorial shelves at Tübingen, Konstanz, Columbia, Harvard and the London School of Economics, he kept the few slim volumes of romantic poetry he had filched then, when he suddenly found himself free to take everything, but with almost nothing to take. This, he taught later, was "entitlement without provisions".

Liberty, he had discovered the hard way, needed institutions to preserve it. All the apparatus of civil society—courts, parliament, written constitutions, citizenship—was needed to ensure, in a favourite phrase, the greatest number of "life-chances", or choices, for everyone. And the nation state, though he was well aware of its parochial and xenophobic limitations, seemed to be liberty's best incubator.

Conflict-management, too, was necessary. The world was not simple. A bland union of wills and ideas led to totalitarianism; a perfect Arcadia would reduce human talents to a dormant state. Only man's "unsocial sociability", in the words of one of his heroes, Immanuel Kant, could sting society towards progress. And in the words of another hero, Karl Popper, at whose feet he sat at the LSE in 1952-53, since no one had found the grail of ultimate wisdom, "let us make sure above all that it remains possible to give different answers". That was why he confronted Rudi Dutschke, leader of Germany's students, on a trailer in Freiburg at the height of the unrest of 1968 (pictured above): not hiding away like Raymond Aron at the Sorbonne, but vigorously debating, professor with student, as he did all his life.

One sharp spat was with Milton Friedman. Liberty required prosperity; and although he was deeply

impressed with Friedman's argument that every government intervention curbed liberty directly, he favoured a basic level of income assured by the state. The word "redistribution" sometimes passed his lips, and he had doubts about Adam Smith's "natural progress of opulence" through the market. At times like these—as when he attacked Thatcherism, and advised his successor at the LSE to "talk to the porters first"—it was clear that Lord Dahrendorf's roots were in the German Social Democratic Party, for which his father was a brave MP in the 1930s. His own short career as a Free Democrat MP, ending with a post in Willy Brandt's government in 1969-70, was based on the hope that a party with the word "Free" in it could best defend democracy. But the FDP, like the Lib Dems in England, which became his adopted country in 1988, was small and weak, and not quite what he wanted. He was, he said, "a bit of a loner"; no party satisfied his restless, hungry and intermittently gloomy spirit.

Straddling the divides

Nor did much else. Though an ardent enthusiast for Europe in principle, his stint as an EEC commissioner in 1970-73 left him appalled by the "perniciousness" of its bureaucracy. He liked social democracy, thought it a good promoter of liberty, urged on its expansion of higher education, but found that this too weltered in bureaucracy in the end. After ten years at the helm of the LSE, a happy time, he nevertheless regretted that he had spent so many hours filling in forms and seeking funds, rather than nourishing the little "corners and pockets of creation" that made the institution both great, and free.

He saw himself first as a straddler—roughly on the scale of the Colossus of Rhodes, for he was not short of self-esteem. His teaching as well as his affections connected Germany, Britain and the United States. His thinking, contained in almost 30 books, might eventually bridge the gap between the haves and the have-nots, or, in his redefinition of the class divide, "order-givers and order-takers". Some sort of balance might also emerge between entitlements and provisions, or citizens' rights and vested interests, without blood running in the streets.

He was less sure he had straddled the divide between thinking and doing, though others thought he had. These were different worlds, and had to be. His own scholar's hopes for such things as a "world civil society" seemed to make the politician in him uncomfortable. Liberty was untidier than that. It was students camped in his LSE office; it was cross-bench voting in the House of Lords, to which he was appointed in 1993; it was his father's passionate underlinings, in red crayon, in Max Weber's "Politics as a Vocation"; it was a schoolboy ripping up his prison mattress in order to write down, defiantly, all the Latin he knew.

Overview

Jun 25th 2009
From The Economist print edition

In **America**, orders for durable goods rose by 1.8% in May after a similar increase in April. Encouragingly, businesses seem more willing to invest, with orders for capital goods rising 9.5% in the month. Sales of new homes fell slightly in May but sales of existing homes perked up by 2.4%. The stock of unsold homes fell, leaving 9.6 months of supply on the market, down from 10.1 months in April.

A measure of **euro-area** activity, based on surveys of purchasing managers in manufacturing and services, edged up to from 44.0 to 44.4 in June. In **Germany**, businessmen are feeling cheerier: the index of business sentiment published by Ifo, a Munich research firm, rose in June from 84.3 to 85.9, the highest level this year. In **France**, household purchases of manufactured goods fell by 0.2% in May, after an increase of 0.5% in April. The value of **Italy's** retail sales fell by 0.4% in May.

Mortgage lending in **Britain** increased by just £2.3 billion in May, according to the British Bankers Association. That was the smallest monthly rise since 2001.

Japan's customs-based trade balance was in surplus for a second consecutive month in May. The value of exports was broadly flat, while that of imports declined by 3.6%.

The National Bank of **Hungary** kept its benchmark interest rate at 9.5% but said that it may cut rates if market sentiment about Hungary's economy remained stable. The Bank of **Israel** kept its main interest rate unchanged at 0.5%.

Output, prices and jobs

Jun 25th 2009
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2009†	2010†	latest	latest	year ago	2009†	rate‡, %
United States	−2.5 Q1	−5.7	−2.8	+1.6	−13.4 May	−1.3 May	+4.2	−0.8	9.4 May
Japan	−8.8 Q1	−14.2	−6.7	+0.8	−30.7 Apr	−0.1 Apr	+0.8	−1.1	5.0 Apr
China	+6.1 Q1	na	+6.5	+7.3	+8.9 May	−1.4 May	+7.7	−0.5	9.0 2008
Britain	−4.1 Q1	−7.4	−3.7	+0.6	−12.3 Apr	+2.2 May§	+3.3	+1.5	7.2 Apr††
Canada	−2.1 Q1	−5.4	−2.3	+1.7	−8.4 Mar	+0.1 May	+2.2	+0.3	8.4 May
Euro area	−4.8 Q1	−9.7	−4.1	+0.5	−21.6 Apr	nil May	+3.7	+0.4	9.2 Apr
Austria	−3.5 Q1	−10.6	−2.6	+0.2	−14.3 Mar	+0.3 May	+3.7	+0.5	4.2 Apr
Belgium	−3.0 Q1	−6.2	−3.3	+0.2	−11.5 Mar	−0.4 May	+5.2	+0.5	11.2 Feb‡‡
France	−3.2 Q1	−4.7	−2.8	+0.5	−18.8 Apr	−0.3 May	+3.3	+0.2	8.9 Apr
Germany	−6.9 Q1	−14.4	−5.5	+0.5	−21.6 Apr	−0.3 Jun	+3.3	+0.2	8.2 May
Greece	+0.3 Q1	−4.6	−3.1	−0.7	−11.7 Apr	+0.5 May	+4.9	+0.4	9.2 Mar
Italy	−6.0 Q1	−10.1	−4.4	+0.3	−24.2 Apr	+0.9 May	+3.6	+0.7	7.3 Q1
Netherlands	−4.5 Q1	−10.7	−3.9	+0.5	−13.2 Apr	+1.6 May	+2.3	+0.9	4.5 May††
Spain	−3.0 Q1	−7.4	−3.5	−0.5	−28.6 Apr	−0.9 May	+4.6	−0.1	18.1 Apr
Czech Republic	−3.4 Q1	−12.9	−3.0	+1.2	−23.2 Apr	+1.3 May	+6.8	+1.9	7.9 May
Denmark	−3.7 Q4	−7.3	−3.5	+0.5	−15.0 Apr†††	+1.3 May	+3.4	+1.0	3.3 Apr
Hungary	−6.7 Q1	−9.6	−6.0	−1.0	−25.3 Apr	+3.8 May	+7.0	+3.3	9.9 Apr††
Norway	+1.5 Q1	−1.8	−2.0	+0.5	−4.0 Apr	+3.0 May	+3.1	+2.0	3.1 Apr***
Poland	+0.8 Q1	na	−0.8	+1.5	−5.2 May	+3.6 May	+4.4	+2.5	10.8 May††
Russia	−9.5 Q1	na	−5.0	+2.0	−17.1 May	+12.3 May	+15.1	+12.1	9.9 May‡‡
Sweden	−6.5 Q1	−3.6	−4.6	+0.9	−21.2 Apr	−0.4 May	+4.0	−0.4	9.0 May‡‡
Switzerland	−2.4 Q1	−16.0	−2.3	+0.3	−9.4 Q1	−1.0 May	+2.9	−0.5	3.5 May
Turkey	−6.2 Q4	na	−4.5	+1.2	−18.5 Apr	+5.2 May	+10.7	+6.2	16.1 Q1‡‡
Australia	+0.4 Q1	+1.5	−0.8	+1.6	−0.7 Q4	+2.5 Q1	+4.2	+1.8	5.7 May
Hong Kong	−7.8 Q1	−16.1	−6.7	+0.9	−10.2 Q1	+0.1 May	+5.6	+1.0	5.3 May††
India	+5.8 Q1	na	+5.5	+6.4	+1.4 Apr	+8.7 Apr	+7.8	+5.2	6.8 2008
Indonesia	+4.4 Q1	na	+2.4	+3.1	+1.5 Apr	+3.8 May	+10.4	+4.2	8.4 Aug
Malaysia	−6.2 Q1	na	−3.0	+1.2	−11.5 Apr	+2.4 May	+3.8	−0.4	3.0 Q4
Pakistan	+5.8 2008**	na	+1.3	+2.3	−20.6 Mar	+14.4 May	+19.3	+12.0	5.6 2007
Singapore	−10.1 Q1	−14.6	−8.6	+1.3	−0.5 Apr	−0.3 May	+7.5	−0.2	3.3 Q1
South Korea	−4.2 Q1	+0.5	−5.0	+0.6	−8.2 Apr	+2.7 May	+4.9	+1.6	3.9 May
Taiwan	−10.2 Q1	na	−6.9	+0.5	−18.2 May	−0.1 May	+3.7	−1.3	5.8 May
Thailand	−7.1 Q1	−7.3	−4.5	+1.9	−9.7 Apr	−3.3 May	+7.6	−1.0	2.1 Apr
Argentina	+2.0 Q1	+0.2	−3.5	+0.5	−1.2 Apr	+5.5 May	+9.1	+7.0	8.4 Q1‡‡
Brazil	−1.8 Q1	−3.3	−1.5	+2.7	−14.8 Apr	+5.2 May	+5.6	+4.7	8.9 Apr‡‡
Chile	−2.1 Q1	−2.4	−1.0	+2.0	−11.1 Apr	+3.0 May	+8.9	+2.4	9.8 Apr†††‡‡
Colombia	−0.7 Q4	−4.1	−2.0	+1.8	+0.4 Mar	+4.8 May	+6.4	+5.2	12.1 Apr††
Mexico	−8.2 Q1	−21.5	−7.1	+2.8	−13.2 Apr	+6.0 May	+4.9	+5.5	5.3 May‡‡
Venezuela	+0.3 Q1	na	−5.5	−5.4	−0.9 Jan	+27.7 May	+31.4	+30.3	8.1 Q1‡‡
Egypt	+4.3 Q1	na	+3.4	+3.1	+5.7 Q4	+10.2 May	+19.7	+9.1	9.4 Q1‡‡
Israel	+0.5 Q1	−3.6	−1.0	+1.6	−7.7 Mar	+2.8 May	+5.4	+2.7	7.6 Q1
Saudi Arabia	+4.2 2008	na	−1.0	+3.1	na	+5.2 Apr	+9.2	+4.3	na
South Africa	−1.3 Q1	−6.4	−1.8	+3.1	+8.4 Apr	+8.0 May	+11.7	+6.6	23.5 Mar‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	−15.1 Q1	na	−13.0	−3.0	−33.7 Apr	−0.3 May	+11.3	nil	11.1 Mar
Finland	−7.6 Q1	−10.3	−5.7	−1.1	−21.0 Apr	nil May	+4.2	+0.3	8.6 May
Iceland	−3.9 Q1	−13.6	−12.1	−0.7	+10.1 2008	+12.2 Jun	+12.7	+12.5	9.1 Apr‡‡
Ireland	−7.5 Q4	−25.7	−7.5	−2.8	−6.7 Mar	−4.7 May	+4.7	−3.5	11.8 May
Latvia	−18.0 Q1	na	−17.0	−4.0	−16.9 Apr	+4.7 May	+17.9	+2.5	17.4 Apr
Lithuania	−13.6 Q1	−35.8	−13.0	−4.5	−25.5 Apr	+5.2 May	+12.0	+5.0	8.7 Apr‡‡
Luxembourg	−5.2 Q4	−16.8	−5.0	−0.9	−38.9 Mar	−0.3 May	+4.0	+0.5	5.5 Apr‡‡
New Zealand	−2.3 Q4	−2.3	−2.7	+0.6	−7.2 Q4	+3.0 Q1	+3.4	+1.4	5.0 Q1
Peru	+3.0 Mar	na	+1.3	+2.6	−13.6 Apr	+4.2 May	+5.4	+3.8	8.5 May‡‡
Philippines	+0.4 Q1	−8.9	−1.8	+2.3	−12.7 Mar	+3.3 May	+9.5	+2.9	7.5 Q2‡‡
Portugal	−3.7 Q1	−6.2	−4.1	−0.3	−9.9 Apr	−1.2 May	+2.8	−0.7	8.9 Q1‡‡
Slovakia	−5.6 Q1	na	−4.0	+0.7	−24.8 Apr	+2.2 May	+4.6	+1.5	11.4 May‡‡
Slovenia	−8.5 Q1	na	−4.0	+0.5	−24.9 Apr	+0.7 May	+6.4	+1.2	8.8 Apr‡‡
Ukraine	+6.9 Q3	na	−10.0	+1.0	−31.8 May	+14.7 May	+31.1	+16.5	2.6 May
Vietnam	+3.1 Q1	na	+2.1	+4.9	+5.4 Apr	+3.9 May	+25.2	+6.0	4.6 2007

*% change on previous quarter, annual rate. †The Economist poll or Economist Intelligence Unit estimate/forecast. ‡National definitions.- §RPI inflation rate -1.1 in May. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. ***Centred 3-month average †††New series

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

The Economist commodity-price index

Jun 25th 2009
From The Economist print edition

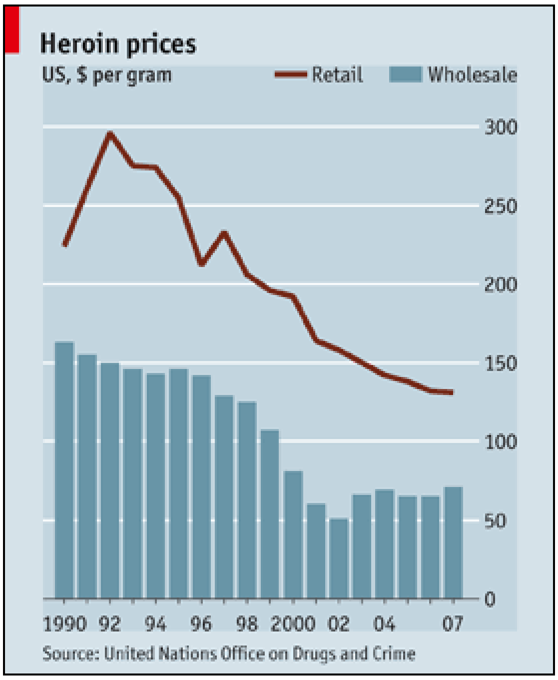
The Economist commodity-price index
2000=100

	Jun 16th	Jun 23rd*	% change on one month	% change on one year
Dollar index				
All items	186.1	181.6	-0.4	-31.8
Food	208.0	204.1	-3.4	-25.0
Industrials				
All	157.7	152.5	+5.2	-41.0
Nfa†	128.7	126.2	-2.5	-38.8
Metals	173.5	166.8	+8.7	-41.8
Sterling index				
All items	171.7	168.8	-2.7	-17.6
Euro index				
All items	123.9	119.9	-0.6	-24.1
Gold				
$ per oz	928.35	922.50	-3.8	+3.7
West Texas Intermediate				
$ per barrel	70.79	68.82	+10.4	-49.8

*Provisional †Non-food agriculturals.

Heroin prices

Jun 25th 2009
From The Economist print edition



The retail and wholesale prices of heroin in America have fallen dramatically since the early 1990s. One gram of heroin in the retail market cost $131 in 2007, the lowest price since UN records began in 1990. The $60 margin between wholesale and retail prices in 2007 was also a record low, suggesting an increasingly competitive retail market. American wholesale prices remain at around twice the level in Western Europe. The UN estimates that annual opiate production—almost all of which is from Afghanistan—jumped to about 8,900 tonnes in 2007, having been flat at around 4,500 tonnes over the previous decade. Seizures of heroin rose to 65 tonnes in 2007 but were still only a small fraction of global production.

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WEEKLY INDICATORS

Trade, exchange rates, budget balances and interest rates

Jun 25th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2009†	Currency units, per $ Jun 24th	Currency units, per $ year ago	Budget balance % of GDP 2009†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−711.0 Apr	−628.3 Q1	−3.2	-	-	−13.2	0.26	3.68
Japan	+6.0 Apr	+111.1 Apr	+1.7	95.4	108	−6.8	0.44	1.38
China	+293.9 May	+426.1 Q4	+7.4	6.83	6.87	−3.8	1.29	3.44
Britain	−150.6 Apr	−44.6 Q4	−1.6	0.61	0.51	−13.9	1.20	3.70
Canada	+28.0 Apr	−3.9 Q1	−1.9	1.15	1.01	−2.3	0.25	3.56
Euro area	−54.7 Apr	−146.2 Apr	−1.0	0.71	0.64	−5.8	1.22	3.45
Austria	−4.2 Mar	+15.0 Q4	+1.7	0.71	0.64	−4.6	1.20	4.22
Belgium	+5.0 Mar	−12.1 Dec	−1.8	0.71	0.64	−4.8	1.21	4.03
France	−78.6 Apr	−63.5 Apr	−2.2	0.71	0.64	−6.6	1.20	3.81
Germany	+205.8 Apr	+178.3 Apr	+4.4	0.71	0.64	−4.6	1.20	3.44
Greece	−58.8 Mar	−45.2 Apr	−8.8	0.71	0.64	−6.0	1.20	5.25
Italy	−13.7 Apr	−70.6 Mar	−2.6	0.71	0.64	−5.2	1.20	4.55
Netherlands	+44.8 Apr	+65.3 Q4	+5.9	0.71	0.64	−4.1	1.20	3.87
Spain	−109.3 Apr	−135.9 Mar	−7.5	0.71	0.64	−9.6	1.20	4.10
Czech Republic	+4.1 Apr	−6.3 Apr	−2.0	18.5	15.5	−4.0	2.13	5.72
Denmark	+7.0 Mar	+7.5 Apr	+1.0	5.31	4.79	−2.5	1.48	3.88
Hungary	+0.6 Apr	−13.0 Q4	−2.9	198	152	−3.9	9.65	10.01
Norway	+65.1 May	+79.6 Q1	+12.5	6.43	5.10	7.2	1.95	4.20
Poland	−18.2 Apr	−19.3 Apr	−5.7	3.22	2.15	−4.0	4.62	6.42
Russia	+141.4 Apr	+75.4 Q1	+0.9	31.2	23.6	−8.0	11.50	10.71
Sweden	+13.1 Apr	+31.4 Q1	+7.3	7.84	6.05	−4.7	0.28	3.51
Switzerland	+17.9 May	+53.3 Q4	+7.6	1.08	1.04	−3.1	0.39	2.36
Turkey	−54.2 Apr	−26.7 Apr	−0.7	1.55	1.22	−5.6	10.37	6.65‡
Australia	+6.1 Apr	−29.8 Q1	−4.7	1.24	1.05	−4.2	3.22	5.62
Hong Kong	−23.8 Apr	+29.3 Q1	+7.7	7.75	7.81	−4.1	0.35	2.61
India	−104.9 Apr	−37.5 Q4	−1.7	48.6	42.7	−7.7	3.35	7.52
Indonesia	+10.4 Apr	−0.8 Q1	+0.9	10,350	9,255	−3.0	7.57	8.04‡
Malaysia	+41.7 Apr	+39.1 Q4	+12.3	3.53	3.26	−7.8	2.09	2.77‡
Pakistan	−17.0 May	−15.3 Q4	−2.1	81.6	67.9	−5.0	12.78	15.39‡
Singapore	+17.0 May	+23.1 Q1	+14.9	1.45	1.37	−4.1	0.50	2.42
South Korea	+7.5 May	+13.2 Apr	+2.9	1,283	1,038	−5.7	2.41	5.11
Taiwan	+12.3 May	+29.2 Q1	+9.6	32.9	30.4	−5.2	0.85	1.44
Thailand	+10.6 May	+7.9 Apr	+5.3	34.1	33.6	−5.6	1.40	3.25
Argentina	+15.8 May	+6.8 Q1	+2.0	3.79	3.01	−1.2	14.63	na
Brazil	+25.6 May	−20.7 May	−1.3	1.96	1.60	−2.0	9.16	6.16‡
Chile	+4.0 May	−4.3 Q1	−1.4	531	507	−3.3	1.32	3.07‡
Colombia	+0.1 Mar	−6.8 Q4	−3.9	2,154	1,778	−3.4	5.54	6.29‡
Mexico	−15.5 May	−14.2 Q1	−3.5	13.3	10.3	−5.4	4.72	8.13
Venezuela	+32.5 Q1	+26.2 Q1	nil	6.50	3.42§	−7.8	14.50	6.55‡
Egypt	−26.8 Q4	−2.9 Q1	−0.8	5.60	5.36	−7.0	10.16	3.27‡
Israel	−10.2 May	+4.1 Q1	+1.7	3.93	3.38	−6.2	0.25	3.91
Saudi Arabia	+197.4 2008	+124.0 2008	−2.1	3.75	3.75	−5.1	0.64	na
South Africa	−6.2 Apr	−18.7 Q1	−5.6	8.04	7.91	−4.0	7.33	8.85
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−2.7 Apr	−1.0 Apr	−3.3	11.2	10.1	−3.7	6.32	na
Finland	+7.5 Mar	+3.4 Apr	+0.6	0.71	0.64	−2.6	1.18	3.88
Iceland	+0.3 May	−6.1 Q1	+3.6	127	81.1	−12.0	7.88	na
Ireland	+45.9 Mar	−12.7 Q4	−2.2	0.71	0.64	−12.6	1.20	5.72
Latvia	−4.6 Apr	−2.3 Apr	−2.0	0.50	0.45	−8.0	21.34	na
Lithuania	−4.8 Apr	−3.0 Apr	−1.8	2.46	2.22	−4.8	8.44	na
Luxembourg	−7.5 Mar	+3.0 Q4	na	0.71	0.64	−3.7	1.20	na
New Zealand	−2.9 Apr	−11.8 Q1	−6.1	1.55	1.32	−6.7	3.80	5.99
Peru	+1.8 Apr	−3.8 Q1	−2.9	3.01	2.97	−2.3	3.05	na
Philippines	−6.9 Apr	+4.2 Dec	+2.7	48.2	44.6	−2.9	3.88	na
Portugal	−31.6 Mar	−27.0 Mar	−9.9	0.71	0.64	−6.0	1.20	4.44
Slovakia	−0.1 Apr	−6.0 Mar	−7.0	21.5	19.5	−5.1	1.35	4.67
Slovenia	−3.8 Apr	−2.4 Mar	−2.5	0.71	0.64	−4.7	1.20	na
Ukraine	−13.4 Q1	−10.1 Q1	−0.3	7.68	4.64	−4.3	9.26	na
Vietnam	−5.0 Jun	−7.0 2007	−10.2	17,773	16,613	−8.8	7.96	7.07

*Merchandise trade only. †The Economist poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.

Markets

Jun 25th 2009
From The Economist print edition

Markets

	Index Jun 24th	% change on one week	Dec 31st 2008 in local currency	Dec 31st 2008 in $ terms
United States (DJIA)	8,299.9	-2.3	-5.4	-5.4
United States (S&P 500)	900.9	-1.1	-0.3	-0.3
United States (NAScomp)	1,792.3	-0.9	+13.7	+13.7
Japan (Nikkei 225)	9,590.3	-2.5	+8.2	+2.9
Japan (Topix)	902.5	-2.2	+5.0	-0.2
China (SSEA)	3,067.9	+4.0	+60.5	+60.2
China (SSEB, $ terms)	184.5	+0.3	+66.6	+66.4
Britain (FTSE 100)	4,280.0	nil	-3.5	+10.7
Canada (S&P TSX)	10,100.9	+0.3	+12.4	+21.1
Euro area (FTSE Euro 100)	744.6	+1.5	-0.2	+0.7
Euro area (DJ STOXX 50)	2,418.5	+1.5	-1.2	-0.3
Austria (ATX)	2,040.2	+1.0	+16.5	+17.6
Belgium (Bel 20)	2,016.4	+2.6	+5.6	+6.6
France (CAC 40)	3,184.8	+0.7	-1.0	-0.1
Germany (DAX)*	4,836.0	+0.8	+0.5	+1.5
Greece (Athex Comp)	2,199.1	+1.7	+23.1	+24.3
Italy (S&P/MIB)	19,040.6	+0.1	-2.2	-1.2
Netherlands (AEX)	254.6	+1.4	+3.5	+4.5
Spain (Madrid SE)	998.5	+3.6	+2.3	+3.3
Czech Republic (PX)	904.7	-1.9	+5.4	+9.8
Denmark (OMXCB)	269.3	nil	+19.1	+20.2
Hungary (BUX)	15,216.7	-0.4	+24.3	+20.1
Norway (OSEAX)	329.0	-2.4	+21.8	+32.6
Poland (WIG)	30,286.4	-2.7	+11.2	+2.4
Russia (RTS, $ terms)	959.2	-7.6	+55.0	+51.8
Sweden (OMXS30)†	783.5	+1.2	+18.3	+19.4
Switzerland (SMI)	5,443.4	+2.7	-1.6	-3.4
Turkey (ISE)	35,758.7	+3.4	+33.1	+32.4
Australia (All Ord.)	3,802.2	-2.6	+3.9	+17.3
Hong Kong (Hang Seng)	17,892.2	-1.1	+24.4	+24.4
India (BSE)	14,422.7	-0.7	+49.5	+50.0
Indonesia (JSX)	1,995.7	-1.4	+47.2	+55.1
Malaysia (KLSE)	1,057.9	-1.2	+20.7	+18.2
Pakistan (KSE)	7,025.9	-0.7	+19.8	+16.2
Singapore (STI)	2,279.0	+0.3	+29.4	+28.2
South Korea (KOSPI)	1,363.8	-2.0	+21.3	+19.0
Taiwan (TWI)	6,380.1	+3.0	+39.0	+38.8
Thailand (SET)	581.4	-0.8	+29.2	+31.8
Argentina (MERV)	1,545.8	+0.7	+43.2	+30.4
Brazil (BVSP)	49,672.0	-2.7	+32.3	+57.1
Chile (IGPA)	14,515.5	-2.3	+28.2	+53.7
Colombia (IGBC)	9,703.3	+1.1	+28.3	+34.0
Mexico (IPC)	23,711.2	-1.8	+5.9	+10.2
Venezuela (IBC)	43,359.4	-0.4	+23.6	+33.0
Egypt (Case 30)	5,586.4	-11.4	+21.5	+19.7
Israel (TA-100)	797.8	+3.2	+41.4	+36.0
Saudi Arabia (Tadawul)	5,609.0	-6.4	+16.8	+16.9
South Africa (JSE AS)	22,391.4	+2.0	+4.1	+19.8
Europe (FTSEurofirst 300)	853.6	+0.9	+2.6	+3.6
World, dev'd (MSCI)	951.1	-0.1	+3.4	+3.4
Emerging markets (MSCI)	741.8	-1.0	+30.8	+30.8
World, all (MSCI)	241.3	-0.2	+6.0	+6.0
World bonds (Citigroup)	796.8	+1.0	-1.6	-1.6
EMBI+ (JPMorgan)	434.6	-0.2	+11.0	+11.0
Hedge funds (HFRX)§	1,074.5	-0.5	+5.3	+5.3
Volatility, US (VIX)	29.1	31.5	40.0	(levels)
CDSs, Eur (iTRAXX)‡	141.7	+5.4	-29.9	-29.2
CDSs, N Am (CDX)‡	197.7	+2.9	-15.3	-15.3
Carbon trading (EU ETS) €	13.3	+3.3	-17.5	-16.7

*Total return index. †New series. ‡Credit-default swap spreads, basis points. Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. §Jun 23rd

World's biggest bank losses

Jun 25th 2009
From The Economist print edition

For many of the world's big commercial banks, 2008 was a rotten year. The 12 largest losses were made by American and European outfits, four of them German. The Royal Bank of Scotland, Citigroup and Wells Fargo suffered a combined loss of more than $160 billion, a sum larger than the GDP of Egypt. Three of the biggest losses were made by banks from Switzerland and Belgium, two fairly small countries. Firms from France and Japan, countries with big banking sectors, are conspicuous by their absence from the list of losses. The three most profitable banks—Industrial and Commercial Bank of China, China Construction Bank and Spain's Santander—together made around $55 billion last year.